

IFRS and US GAAP similarities and differences

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The heart of the matter

**US financial reporting
will undergo an
unprecedented level of
change over the next
several years.**

International Financial Reporting Standards (IFRS) have been affecting US companies for some time, whether through their business dealings with non-US customers and vendors that use IFRS or through their non-US subsidiaries' adoption of IFRS. Soon, US companies will feel an increasing effect of IFRS here at home as key aspects of United States generally accepted accounting principles (US GAAP) and IFRS continue to converge.

The Securities and Exchange Commission's (SEC) proposed roadmap for adopting IFRS slates initial adoption for 2014. That date is apt to slide back somewhat as the SEC continues to focus on economic and regulatory structural concerns as well as the politics of change. We expect the SEC will begin refocusing on IFRS in the fourth quarter of 2009 and/or early 2010.

Despite this delay, the US government's acknowledgment of the need for a single set of high-quality global standards—in addition to the continuing globalization of the capital markets—and the SEC's ongoing, thoughtful approach to assessing IFRS adoption, point to the inevitability of IFRS as the global standard.

Converge → Adopt

In the meantime, it has been proposed that nearly a dozen new standards will advance the convergence of US GAAP and IFRS by the end of 2011. Fundamental areas to be affected by convergence include debt and equity, revenue, leasing, consolidation, and financial instruments.

As converged standards are introduced, many US companies and their investors will see, among other things, major changes in financial statements.

The impact of the accounting changes caused by convergence will go well beyond financial reporting. Tax policy, mergers and acquisitions, financial planning, systems requirements, and compensation structures are just some of the areas that will be affected.

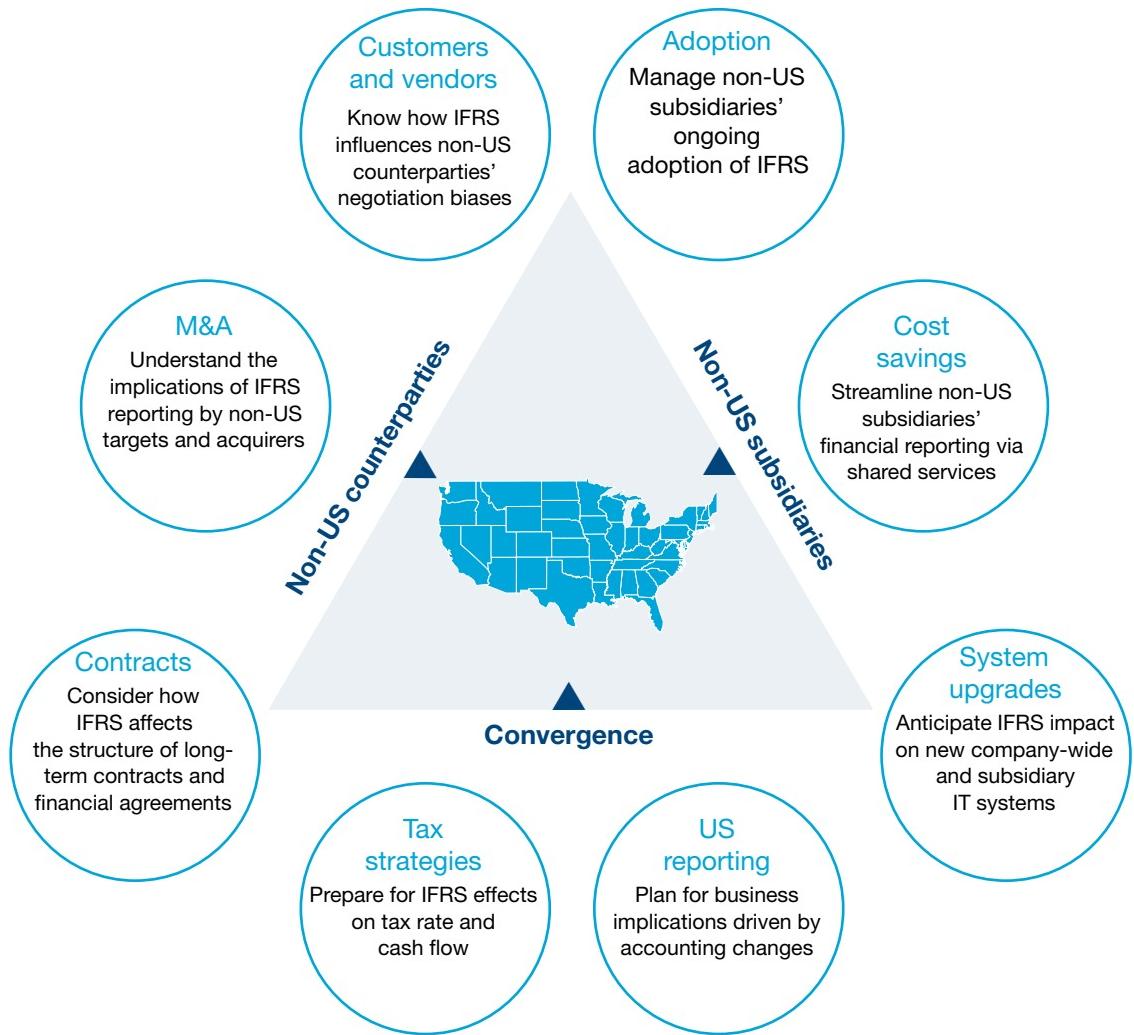
This publication is designed to help readers develop a broad understanding of the major differences between IFRS and US GAAP today as well as an appreciation for the level of change on the horizon. While this publication does not cover every difference between IFRS and US GAAP, it focuses on those PwC generally considers most significant and/or most common.

An in-depth discussion

Examining the implications.

IFRS affects US businesses in multiple ways

The graphic below illustrates a number of the ways in which IFRS affects US businesses. Each of these is expanded upon within the ensuing discussion.



Non-US subsidiaries

Many US multinationals have already been dealing with the effects of IFRS as a result of their foreign subsidiaries. A working understanding of IFRS and careful planning can help to ensure that pitfalls are avoided and benefits are maximized.

Adoption

- Many countries require or permit IFRS for statutory financial reporting purposes, and many more countries plan to follow suit, particularly now that the International Accounting Standards Board (IASB) recently issued a version of IFRS tailored to small and medium-sized entities. This simplified version of IFRS may, assuming certain conditions are met, become available to subsidiaries whose parents use full IFRS, US GAAP or any other financial reporting framework.
- Multinational companies will need to closely manage the process of IFRS adoption by their non-US subsidiaries. Once a subsidiary makes an accounting policy election under IFRS (upon adoption), that decision typically cannot be undone (for statutory reporting purposes), unless the change results in more relevant and reliable information.
- But adoption elections that subsidiaries deem best for themselves won't necessarily be best for their US parents. And, those elections may vary widely among subsidiaries of a given company.
- US multinationals, therefore, need to pay attention to, and actively participate in, their subsidiaries' IFRS adoption, to avoid the unnecessary reporting complexity that divergent policy elections will create, and ultimately to maximize the advantages of being on one set of global accounting standards.

Cost savings

Taking a centralized approach to IFRS adoption (and thereby achieving consistent application across the organization—for both corporate external reporting and local statutory reporting) can create significant cost savings for multinational companies. For example, parent companies might decide to use global shared-services centers to facilitate reporting, consequently reducing the work that goes into financial statement processing, as well as the need to maintain separate sets of accounting records in multiple locations.

System upgrades/implications

As companies prepare to upgrade existing IT systems or implement new ones, they should carefully evaluate whether the systems can handle increased disclosure under IFRS and dual-reporting requirements (companies may need to prepare financial information under both IFRS and US GAAP during the transition period or after their non-US subsidiaries have begun reporting under IFRS). Companies considering new IT systems or system upgrades should assess IFRS capabilities in conjunction with these system changes.

Also, under IFRS, companies may find a change in the amount and type of information they need for external reporting. Identifying potential data gaps early will allow companies to design IT systems that deliver the necessary information efficiently.

Convergence leading to a conversion

The impact of the accounting changes caused by convergence or IFRS adoption will be significant and will have broad-based implications.

US reporting

IFRS has already influenced US GAAP. The effect of that influence will grow over the next several years.

Under the Memorandum of Understanding (MoU) as updated by the Financial Accounting Standards Board (FASB) and the IASB in 2008, the standard setters put forth milestones on the 11 major joint projects listed below:

- Business combinations
- Financial instruments
- Financial statement presentation
- Intangible assets
- Leases
- Liabilities and equity distinctions
- Revenue recognition
- Consolidation
- Derecognition
- Fair value measurement
- Postemployment benefits (including pensions)

Most of these projects are slated for completion by 2011.

The first of these projects resulted in the issuance of new US GAAP business combinations guidance that was effective for fiscal years beginning after December 15, 2008. The new guidance introduced significant changes in the accounting and reporting of business acquisitions and noncontrolling interests in a subsidiary. For example, the new guidance requires that companies record acquisition-related restructuring costs and transaction costs as

current period costs (rather than as a part of purchase price).

US GAAP and IFRS will clearly change as a result of the convergence process. In relation to business combinations, US GAAP was heavily influenced by and moved closer to IFRS.

Consider revenue recognition: The proposed revenue recognition model within the recently released discussion paper is very different from what US companies have long been following.

For instance, under current guidance, warranty obligations are recorded as a cost accrual at the time of sale. Such warranties may be a separate performance obligation under the proposed model and would result in revenue deferral as opposed to cost accrual. At the same time, sales-type incentives such as free products or customer loyalty programs are currently recognized as marketing expense in some circumstances. The proposed model would generally require that those incentives be considered performance obligations and revenue deferred until such obligations are satisfied, as when a customer redeems loyalty points. This change would align US GAAP with the guidance for customer loyalty programs under IFRS. In general, the proposal will drive an increase in the identification and separation of performance obligations, which may require greater use of estimates than is the case under current practice. How a company recognizes revenue can affect a host of other things, including sales strategy, salesperson compensation, cash management, investor communications, and even information-system design.

Lease arrangements are another area that will be affected by the convergence agenda. The standard setters recently released a discussion paper on preliminary views for the future of lease accounting for lessees. Under the proposed model the operating lease accounting model would be

eliminated. As such, all rights and obligations under lease arrangements would be accounted for as assets and liabilities—this represents a major change from current practice.

The recognition of assets and liabilities for all leases currently considered to be operating in nature would impact balance sheet metrics/ratios as well as income statement presentation. Such treatment also could cause lessees to modify their business practices, because customers often have one budget for operating expenses and another budget for capital expenses, with responsibility for each budget overseen by different buyers in the customer's organization.

The proposal also would require significant ongoing monitoring efforts as lessees would be required to reassess the lease term, contingent rentals, residual value guarantees and the corresponding accounting at each reporting date using current facts and circumstances.

Tax strategies

Companies need to assess how IFRS-driven changes in financial reporting (both US and statutory) are apt to affect taxes.

IFRS adoption can impact the effective tax rate. For example, in adopting IFRS, a company may find that its debt-equity levels are affected, thereby limiting, or increasing, the amount of interest that may be deductible in a jurisdiction, with a related impact on the company's effective tax rate. There are also potentially significant cash tax implications. In some jurisdictions, tax reporting aligns with statutory reporting. When IFRS is adopted for statutory reporting purposes in such a location the impact can be significant.

These changes will be increasingly pervasive as more countries adopt IFRS for statutory accounting purposes outside the United States. Consequently, companies must consider how their current tax structuring might be affected, as well as any further tax planning. They should also assess the potential tax impact of upcoming converged standards (not just the impact of eventual IFRS adoption) and devise appropriate tax planning strategies.

Contracts

Adopting IFRS will have an impact on long-term contracts and financial agreements. For example, a company's debt covenants may specify a certain debt/equity ratio, which may change once the company applies newly converged standards or adopts IFRS, hence making it necessary for the company to renegotiate its debt agreements. Another example, as referenced above, is that rights and obligations resulting from current operating leases may need to be accounted for as assets and liabilities, thereby significantly changing balance sheet, income statement and cash flow presentation, and key metrics.

Another consideration is that compensation and bonus arrangements are often linked to financial metrics reported under US GAAP. Those metrics will change when the converged standards take effect and, ultimately, when the United States adopts IFRS. Anticipating the effects of these changes will help companies ensure that they meet their external reporting objectives.

Mergers & Acquisitions

Global consolidation is expected to continue. As more countries adopt IFRS for capital market and statutory reporting purposes, knowledge and understanding of IFRS will be increasingly important for US companies as they conduct their due diligence in evaluating public and private non-US targets. Conversely, US companies that are targets may need to quickly share IFRS-based data with a potential buyer.

Customers and vendors

More and more US companies transact with global customers and suppliers, many of which are located in countries where IFRS is the primary reporting language. A sound understanding of how IFRS affects the behavior of customers and vendors will better position US companies in business negotiations with those counterparties.

What this means for your business

A call to action.

What companies can and should do now

Independent of when the United States ultimately adopts IFRS, those standards are already having a significant impact on US businesses. The impact will only increase in the next several years as convergence takes place and adoption of IFRS gains momentum.

In the near term, four main challenges require companies' attention on the IFRS front:

- Keeping pace with an unprecedented rate of financial reporting change as converged standards roll out in roughly a dozen key areas between now and the end of 2011
- Monitoring and managing subsidiaries' adoption of IFRS as more countries move to a single set of global reporting standards
- Understanding the ways in which the structure of deals and transactions with non-US counterparties (particularly vendors and customers) may be influenced by those counterparties' increased interest in IFRS accounting outcomes
- Continued focus on differences between IFRS and US GAAP, since convergence projects will not eliminate all current differences between the two sets of standards

To successfully face these challenges, companies should:

- Assess the potential impact of convergence and, ultimately, of IFRS adoption:
 - Contemplate using scenario planning to help incorporate likely convergence and IFRS adoption outcomes into strategic thinking and business planning
 - Assess how the changes will affect the company's reporting, long-term contractual commitments, tax structures, financing, systems, and controls
 - Consider how the actual accounting changes will influence customers and vendors
- Oversee subsidiary adoption of IFRS: Closely monitor non-US subsidiaries' accounting policy elections as they adopt IFRS. Influence subsidiaries' transition timing and strategies.

By staying focused on aspects of convergence and adoption that have a long lead-time, companies can stay ahead of the game, while also pursuing small one-off projects and "easy wins" where desirable.

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A further study
IFRS and US GAAP
similarities and differences

About this publication

This publication is designed to alert companies to the timing and scope of accounting changes that the US GAAP/IFRS convergence agenda and the eventual adoption of IFRS in the United States will bring. It is also designed to put into context how convergence with or adoption of IFRS has ramifications far beyond the accounting department.

With the stage having been set, the remainder of this publication contains "A further study" consisting, for each topical area, of:

- An executive summary of current IFRS and US GAAP differences and the potential implications thereof,
- A more detailed analysis of current differences between the frameworks including an assessment of the impact embodied within the differences, and
- Commentary/insight with respect to recent/proposed guidance including developments in relation to the overall convergence agenda.

In addition to the above, this publication also includes an overview of the new IFRS for Small and Medium-sized Entities (IFRS for SMEs) as well as the US GAAP codification project.

This publication takes into account authoritative pronouncements and other developments under IFRS and US GAAP up to June 30, 2009. This publication is not all-encompassing. When applying the individual accounting frameworks, companies should consult all of the relevant accounting standards and, where applicable, national law.

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IFRS first-time adoption

IFRS 1, *First-Time Adoption of International Financial Reporting Standards*, is the guidance that is applied during preparation of a company's first IFRS-based financial statements. IFRS 1 was created to help companies transition to IFRS and provides practical accommodations intended to make first-time adoption cost-effective. It also provides application guidance for addressing difficult conversion topics.

This section is intended to provide an overview of the standard. PricewaterhouseCoopers' publication, *Adopting IFRS*, serves as an excellent companion piece to this guide by helping companies understand, in greater detail, the requirements of IFRS 1 and by providing answers to common questions in relation to the implementation of IFRS.

What is IFRS 1?

The key principle of IFRS 1 is full retrospective application of all IFRS standards that are effective as of the closing balance sheet or reporting date of the first IFRS financial statements. IFRS 1 requires companies to:

- Identify the first IFRS financial statements;
- Prepare an opening balance sheet at the date of transition to IFRS;
- Select accounting policies that comply with IFRS and to apply those policies retrospectively to all of the periods presented in the first IFRS financial statements;
- Consider whether to apply any of the 15 optional exemptions from retrospective application;
- Apply the four mandatory exceptions from retrospective application; and
- Make extensive disclosures to explain the transition to IFRS.

There are 15 optional exemptions to ease the burden of retrospective application. There are also four mandatory exceptions where retrospective application is not permitted. The exemptions provide limited relief for first-time adopters, mainly in areas where the information needed to apply IFRS retrospectively may be most challenging to obtain. There are, however, no exemptions from the disclosure requirements of IFRS, and companies may experience challenges in collecting new information and data for retrospective footnote disclosures.

Many companies will need to make significant changes to existing accounting policies in order to comply with IFRS, including in such key areas as revenue recognition, inventory accounting, financial instruments and hedging, employee benefit plans, impairment testing, provisions and stock-based compensation.

When to apply IFRS 1

Companies will apply IFRS 1 when they transition from their previous Generally Accepted Accounting Principles (GAAP) to IFRS and prepare their first IFRS financial statements. These are the first financial statements to contain an explicit and unreserved statement of compliance with IFRS.

The opening IFRS balance sheet

The opening IFRS balance sheet is the starting point for all subsequent accounting under IFRS and is prepared at the date of transition, which is the beginning of the earliest period for which full comparative information is presented in accordance with IFRS. For example, preparing IFRS financial statements for the three years ending December 31, 2014, would have a transition date of January 1, 2012. That would also be the date of the opening IFRS balance sheet.

IFRS 1 requires that the opening IFRS balance sheet:

- Include all of the assets and liabilities that IFRS requires;
- Exclude any assets and liabilities that IFRS does not permit;
- Classify all assets, liabilities and equity in accordance with IFRS;
- Measure all items in accordance with IFRS; and
- Be prepared and presented within an entity's first IFRS financial statements.

These general principles are followed except where one of the optional exemptions or mandatory exceptions does not require or permit recognition, classification, and measurement in accordance with IFRS.

Some important takeaways

The transition to IFRS can be a long and complicated process with many technical and accounting challenges to consider. Experience with conversions in Europe and Asia indicates there are some challenges that are consistently underestimated by companies making the change to IFRS, including:

Consideration of data gaps—Preparation of the opening IFRS balance sheet may require the calculation or collection of information that was not previously required under US GAAP. Companies should plan their transition and identify the differences between IFRS and US GAAP early so that all of the information required can be collected and verified in a timely way. Likewise, companies should also identify differences between local regulatory requirements and IFRS. This could also impact the amount of information-gathering necessary. For example, certain information required by the SEC but not by IFRS (e.g., a summary of historical data) can still be presented, in part, under US GAAP but must be clearly labeled as such, and the nature of the main adjustments to comply with IFRS must be discussed. Other incremental information required by a regulator may need to be presented in accordance with IFRS. The SEC currently envisions, for example, two years of comparative IFRS financial statements whereas IFRS would require only one.

Consolidation of additional entities—IFRS consolidation principles differ from those of US GAAP, and those differences may cause some companies to consolidate entities that were not consolidated under US GAAP. Subsidiaries that were previously excluded from the consolidated financial statements are to be consolidated as if they were first-time adopters on the same date as the parent. Companies will also have to consider the potential data gaps of investees in order to comply with IFRS informational and disclosure requirements.

Consideration of accounting policy choices—A number of IFRS standards allow companies to choose between alternative policies. Companies should select carefully the accounting policies to be applied to the opening balance sheet and have a full understanding of the implications to current and future periods. Companies should take this opportunity to evaluate their IFRS accounting policies with a clean-sheet-of-paper mind-set. Although many accounting policies are similar between US GAAP and IFRS, companies should not overlook the opportunity to explore alternative IFRS accounting policies that may better reflect the economic substance of their transactions and enhance their communications with investors.

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Revenue recognition

Revenue recognition

US GAAP revenue recognition guidance is extensive and includes a significant number of standards issued by the Financial Accounting Standards Board (FASB), the Emerging Issues Task Force (EITF), the American Institute of Certified Public Accountants (AICPA) and the US Securities and Exchange Commission (SEC). The guidance tends to be highly detailed and is often industry-specific. While the FASB's codification project has put authoritative US GAAP in one place, it was not intended to impact the volume and/or nature of the guidance. IFRS has two primary revenue standards and four revenue-focused interpretations. The broad principles laid out in IFRS are generally applied without further guidance or exceptions for specific industries.

A detailed discussion of industry-specific differences is beyond the scope of this publication. However, for illustrative purposes only, we note that US GAAP guidance on software revenue recognition requires the use of vendor-specific objective evidence (VSOE) of fair value before revenue can be recognized. IFRS does not have an equivalent requirement. We also observe that the many pieces of industry-specific US GAAP guidance can produce conflicting results, within US GAAP, for economically similar transactions. For example, activation services provided by telecommunications providers are often economically similar to connection services provided by cable television companies. The US GAAP guidance governing the accounting for these transactions, however, differs. The result is that the timing of revenue recognition for these economically similar transactions also varies. As noted above, IFRS contains minimal industry specific guidance. Rather, the broad principles-based approach of IFRS is to be applied across entities and industries.

A few of the more significant, broad-based differences have been highlighted below:

The topic of pricing contingencies and how they factor into the revenue recognition models varies between US GAAP and IFRS. Under US GAAP, revenue recognition is based on fixed or determinable pricing criterion, which results in contingent amounts not being recorded as revenue until the contingency is resolved. IFRS generally looks to the probability of economic benefits associated with the transaction flowing to the entity and the ability to reliably measure the revenue in question, including any contingent revenues. This could lead to differences in the timing of revenue recognition with revenue potentially being recognized earlier under IFRS.

One of the most common general revenue recognition issues has to do with (1) the determination of when transactions with multiple deliverables should be separated into components and (2) with the way revenue gets allocated to the different components. While the broad concepts in this area are similar and often result in similar conclusions under both US GAAP and IFRS, the potential for significantly different conclusions also exists. US GAAP focuses on detailed separation and allocation criteria, whereas IFRS focuses on the economic substance of the transaction(s). For example, US GAAP separation criteria indicate that VSOE of fair value is preferable in all circumstances in which it is available. When VSOE is not available, third-party vendor objective evidence may be used. Consideration should be allocated based on relative fair value, but may be allocated based on the residual method if the fair value of the delivered item is unknown. IFRS is not as restrictive in terms of how to obtain sufficient evidence of fair value. For example, IFRS allows the use of cost plus a reasonable margin to determine fair value, which is typically not allowed for US GAAP purposes. This could lead to differences between the two standards in both the separation and allocation of consideration in multiple deliverable arrangements. The US GAAP guidance in relation to multiple-element arrangements is in the process of being revisited. While some differences may be eliminated as part of the update process, new differences may be created.

The accounting for customer loyalty programs may drive fundamentally different results. The IFRS requirement to treat customer loyalty programs as multiple-element arrangements, in which consideration is allocated to the goods or services and the award credits based on fair value through the eyes of the customer, would be acceptable for US GAAP purposes. Some US GAAP reporting companies, however, use the incremental cost model, which is very different from the multiple-element approach required under IFRS. In this instance the implication is that IFRS generally results in the deferral of more revenue and profit.

For service transactions, US GAAP prohibits use of the cost-to-cost percentage-of-completion method (unless the transaction explicitly qualifies as a particular type of construction or production contract). Most service transactions that do not qualify for these types of construction contracts are accounted for by using a proportional-performance model. IFRS requires use of the percentage-of-completion method in recognizing revenue under service arrangements unless progress toward completion cannot be estimated reliably (in which case a zero-profit approach is used) or a specific act is much more significant than any other (in which case revenue recognition is postponed until the act is executed). Diversity in application of the percentage-of-completion method may also result in differences.

Another difference involves construction contracts because IFRS prohibits use of the completed-contract method. This may, depending on the specific facts and circumstances, result in the acceleration of revenue recognition under IFRS.

In general, due to the significant differences in the overall volume of revenue-related guidance, a detailed analysis of specific fact patterns is necessary to identify and evaluate the potential differences between the accounting frameworks.

While each of the standard setters continues to make isolated changes to their individual accounting frameworks, they are also working together on a number of joint projects. In December 2008, a joint discussion paper titled *Preliminary Views on Revenue Recognition in Contracts with Customers* was issued by the IASB and the FASB. The model outlined in the discussion paper would have a significant impact on current revenue recognition under both IFRS and US GAAP. Every industry within the scope of the project may be impacted to some extent, and some will see pervasive changes.

Further details on the foregoing and other selected differences are described in the following table.

Impact	US GAAP	IFRS
<p>Revenue recognition—general</p> <p>The concept of IFRS being principles-based and US GAAP being principles-based, but also rules laden, is perhaps nowhere more evident than in the area of revenue recognition.</p> <p>This fundamental difference requires a detailed, transaction-based analysis to identify the potential GAAP differences.</p> <p>Those differences may have ramifications on how companies operate, including, for example, how they bundle various products and services in the marketplace.</p>	<p>Revenue recognition guidance is extensive and includes a significant volume of literature issued by various US standard setters.</p> <p>Generally, the guidance focuses on revenues being (i) either realized or realizable and (ii) earned. Revenue recognition is considered to involve an exchange transaction; that is, revenue should not be recognized until an exchange transaction has occurred.</p> <p>These rather straightforward concepts are, however, augmented with detailed rules.</p> <p>A detailed discussion of industry-specific differences is beyond the scope of this publication. However, for illustrative purposes only, we note that highly specialized guidance exists for software revenue recognition. One aspect of that guidance focuses on the need to demonstrate VSOE of fair value in order to separate different software elements. This requirement goes beyond the general fair value requirement of US GAAP.</p>	<p>Two primary revenue standards capture all revenue transactions within one of four broad categories:</p> <ul style="list-style-type: none"> • Sale of goods • Rendering of services • Others' use of an entity's assets (yielding interest, royalties, etc.) • Construction contracts <p>Revenue recognition criteria for each of these categories include the probability that the economic benefits associated with the transaction will flow to the entity and that the revenue and costs can be measured reliably. Additional recognition criteria apply within each broad category.</p> <p>The principles laid out within each of the categories are generally to be applied without significant further rules and/or exceptions.</p> <p>The concept of VSOE of fair value does not exist under IFRS, thereby resulting in a lower fair value separation threshold for software under IFRS.</p> <p>While the price that is regularly charged by an entity when an item is sold separately is the best evidence of the item's fair value, IFRS acknowledges that reasonable estimates of fair value (such as cost plus a margin) may, in certain circumstances, be acceptable alternatives.</p>

Impact	US GAAP	IFRS
<p>Contingent consideration—general</p> <p>Revenue may be recognized earlier under IFRS when there are contingencies associated with the price/level of consideration.</p>	<p>General guidance associated with contingencies around consideration is addressed within SAB Topic 13 and the concept of the seller's price to the buyer being fixed or determinable.</p> <p>Even when delivery has clearly occurred (or services have clearly been rendered) the SEC has emphasized that revenue related to contingent consideration should not be recognized until the contingency is resolved. It would not be appropriate to recognize revenue based upon the probability of a factor being achieved.</p>	<p>For the sale of a good, one looks to the general recognition criteria as follows:</p> <ul style="list-style-type: none"> • The entity has transferred to the buyer the significant risks and rewards of ownership; • The entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold; • The amount of revenue can be measured reliably; • It is probable that the economic benefits associated with the transaction will flow to the entity; and • The costs incurred or to be incurred in respect of the transaction can be measured reliably. <p>As such, assuming that the other revenue recognition criteria are met, IFRS specifically calls for consideration of the probability of the benefits flowing to the entity as well as the ability to reliably measure the associated revenue. If it were not probable that the economic benefits would flow to the entity or if the amount of revenue could not be reliably measured, recognition of the contingent portion would be postponed until such time as all of the criteria are met.</p>

Impact	US GAAP	IFRS
<p>Multiple-element arrangements—general</p> <p>While the guidance often results in the same treatment under the two frameworks, careful consideration is required, as there is the potential for significant differences.</p> <p>Where differences do exist, IFRS may result in the separation of more components/elements, which may result in earlier revenue recognition.</p>	<p>Revenue arrangements with multiple deliverables are separated into different units of accounting if the deliverables in the arrangement meet all of the specified criteria outlined in the guidance. Revenue recognition is then evaluated independently for each separate unit of accounting.</p> <p>The US GAAP concept of separating potential units of accounting and identifying/measuring the fair value of a potential unit of accounting looks to market indicators of fair value and generally does not allow, for example, an estimated internal calculation of fair value based on costs and an assumed or reasonable margin.</p> <p>When there is objective and reliable evidence of fair value for all units of accounting in an arrangement, the arrangement consideration should be allocated to the separate units of accounting based on their relative fair values.</p> <p>When fair value is known for the undelivered items, but not for the delivered item, a residual approach can be used.</p>	<p>The revenue recognition criteria are usually applied separately to each transaction. In certain circumstances, however, it is necessary to separate a transaction into identifiable components in order to reflect the substance of the transaction. When identifiable components have stand-alone value and their fair value can be measured reliably, separation is appropriate.</p> <p>At the same time, two or more transactions may need to be grouped together when they are linked in such a way that the commercial effect cannot be understood without reference to the series of transactions as a whole.</p> <p>The price that is regularly charged when an item is sold separately is the best evidence of the item's fair value. At the same time, under certain circumstances, a cost-plus-reasonable-margin approach to estimating fair value would be appropriate under IFRS. Under rare circumstances, a reverse residual methodology may be acceptable.</p>

Impact	US GAAP	IFRS
Multiple-element arrangements—general (continued)	<p>The reverse-residual method—when objective and reliable evidence of the fair value of an undelivered item or items does not exist—is precluded unless other US GAAP guidance specifically requires the delivered unit of accounting to be recorded at fair value and marked to market each reporting period thereafter.</p> <p>Refer to the Recent/proposed Guidance section below for proposed changes to US GAAP multiple-element arrangements guidance.</p>	<p>The use of either the cost-plus or the reverse residual method under IFRS may allow for the separation of more components/elements than would be achieved under US GAAP.</p>
Multiple-element arrangements—contingencies In situations where the amount allocable to a delivered item includes an amount that is contingent on the delivery of additional items, differences in the frameworks may result in recognizing a portion of revenue sooner under IFRS.	<p>The guidance includes a strict limitation on the amount of revenue otherwise allocable to the delivered element in a multiple-element arrangement.</p> <p>Specifically, the amount allocable to a delivered item is limited to the amount that is not contingent on the delivery of additional items. That is, the amount allocable to the delivered item or items is the lesser of the amount otherwise allocable in accordance with the standard or the noncontingent amount.</p>	<p>IFRS maintains its general principles and would look to key concepts including, but not limited to, the following:</p> <ul style="list-style-type: none"> • Revenue should not be recognized before it is probable that economic benefits would flow to the entity. • The amount of revenue can be measured reliably. <p>When a portion of the amount allocable to a delivered item is contingent on the delivery of additional items, IFRS might not impose a limitation on the amount allocated to the first item. A thorough consideration of all factors would be necessary so as to draw an appropriate conclusion. Factors to consider would include the extent to which fulfillment of the undelivered item is within the control of, and is a normal/customary deliverable for, the selling party as well as the ability and intent of the selling party to enforce the terms of the arrangement. In practice, the potential limitation is often overcome.</p>

Impact	US GAAP	IFRS
<p>Multiple-element arrangements—customer loyalty programs</p> <p>Entities that grant award credits as part of sales transactions, including awards that can be redeemed for goods and services not supplied by the entity, may encounter differences that impact both the timing and total value of revenue to be recognized.</p> <p>Where differences exist, revenue recognition is likely to be delayed under IFRS.</p>	<p>Currently, divergence exists under US GAAP in the accounting for customer loyalty programs. There are two very different models that are generally employed.</p> <p>Some companies utilize a multiple-element accounting model, wherein revenue is allocated to the award credits based on relative fair value. Other companies utilize an incremental cost model, wherein the cost of fulfillment is treated as an expense and accrued for as a “cost to fulfill,” as opposed to deferred based on relative fair value.</p> <p>The two models can result in significantly different accounting.</p>	<p>IFRS requires that award, loyalty or similar programs, whereby a customer earns credits based on the purchase of goods or services, be accounted for as multiple-element arrangements. As such, IFRS requires that the fair value of the award credits (otherwise attributed in accordance with the multiple-element guidance) be deferred and recognized separately upon achieving all applicable criteria for revenue recognition.</p> <p>The above-outlined guidance applies whether the credits can be redeemed for goods or services supplied by the entity or whether the credits can be redeemed for goods or services supplied by a different entity. In situations where the credits can be redeemed through a different entity, a company should also consider the timing of recognition and appropriate presentation of each portion of the consideration received given the entity's potential role as an agent versus as a principal in each aspect of the transaction.</p>

Impact	US GAAP	IFRS
<p>Multiple element arrangements—loss on delivered element only</p> <p>The timing of revenue and cost recognition in situations with multiple element arrangements and losses on the first element may vary under the two frameworks.</p>	<p>When there is a loss on the first element of a two element arrangement within the scope of ASC 605-25 an accounting policy choice may exist.</p> <p>When there is a loss on the first element but a profit on the second element (and the overall arrangement is profitable) a company has an accounting policy choice if performance of the undelivered element is both probable and in the company's control. Specifically, there are two acceptable ways of treating the loss incurred in relation to the delivered unit of accounting. The company may: a) recognize costs in an amount equal to the revenue allocated to the delivered unit of accounting and defer the remaining costs until delivery of the second element, or b) recognize all costs associated with the delivered element (i.e., recognize the loss) upon delivery of that element.</p>	<p>When there is an apparent loss on the first element of a two element arrangement an accounting policy choice may exist as of the date the contract was entered into.</p> <p>When there is a loss on the first element but a profit on the second element (and the overall arrangement is profitable) a company has an accounting policy choice if performance of the undelivered element is both probable and in the company's control. Specifically, there are two acceptable approaches. The company may: a) determine that revenue is more appropriately allocated based upon cost plus a reasonable margin thereby removing the loss on the first element or b) recognize all costs associated with the delivered element (i.e., recognize the loss) upon delivery of that element.</p> <p>Once the initial allocation of revenue has been made, it would not be revisited. That is, if the loss on the first element became apparent only after the initial revenue allocation, the revenue allocation could not be revisited.</p> <p>There would not, under IFRS, be support for simply deferring the loss on the first element akin to the US GAAP approach.</p>

Impact	US GAAP	IFRS
<p>Sales of services—general</p> <p>A fundamental difference in the guidance surrounding how service revenue should be recognized has the potential to significantly impact the timing of revenue recognition.</p>	<p>US GAAP prohibits the use of the cost-to-cost percentage-of-completion method to recognize revenue under service arrangements unless the contract is within the scope of specific guidance for construction or certain production-type contracts.</p> <p>Generally, companies would have to apply the proportional-performance model or the completed-performance model. In circumstances where output measures do not exist, input measures, which approximate progression toward completion, may be used. Revenue is recognized based on a discernible pattern and if none exists, then the straight-line approach may be appropriate.</p> <p>Revenue is deferred where the outcome of a service transaction cannot be measured reliably.</p>	<p>IFRS requires that service transactions be accounted for by reference to the stage of completion of the transaction. This method is often referred to as the percentage-of-completion method. The stage of completion may be determined by a variety of methods (including the cost-to-cost method). Revenue may be recognized on a straight-line basis if the services are performed by an indeterminate number of acts over a specified period of time and no other method better represents the stage of completion.</p> <p>When the outcome of a service transaction cannot be measured reliably, revenue may be recognized to the extent of recoverable expenses incurred. That is, a zero-profit model would be utilized, as opposed to a completed-performance model. If the outcome of the transaction is so uncertain that recovery of costs is not probable, revenue would need to be deferred until a more accurate estimate could be made.</p> <p>Revenue may have to be deferred in instances where a specific act is much more significant than any other acts.</p>

Impact	US GAAP	IFRS
<p>Sales of services—right of refund</p> <p>Differences within the models provide the potential for revenue to be recognized earlier under IFRS when services-based transactions include a right of refund.</p>	<p>A right of refund may preclude recognition of revenue from a service arrangement until the right of refund expires.</p> <p>In certain circumstances, companies may be able to recognize revenue over the service period—net of an allowance—if certain criteria within the guidance are satisfied.</p>	<p>Service arrangements that contain a right of refund must be considered in order to determine whether the outcome of the contract can be estimated reliably and whether it is probable that the company would receive the economic benefit related to the services provided.</p> <p>When reliable estimation is not possible, revenue is recognized only to the extent of the costs incurred that are probable of recovery.</p>
<p>Construction contracts</p> <p>There are a variety of differences with potentially far-reaching consequences.</p> <p>Differences ranging from the transactions scoped into the construction contract accounting guidance in both frameworks to the actual application of the models may result in significant impacts.</p>	<p>The guidance applies to accounting for performance of contracts for which specifications are provided by the customer for the construction of facilities or the production of goods or the provision of related services.</p> <p>The scope of this guidance has generally been limited to certain specific industries and types of contracts.</p>	<p>The guidance applies to the fixed-price and cost-plus-construction contracts of contractors for the construction of a single asset or a combination of assets that are interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use. The guidance is not limited to certain industries.</p> <p>Assessing whether a contract is within the scope of the construction contract standard or the broader revenue standard has been an area of recent focus. A buyer's ability to specify the major structural elements of the design (either before and/or during construction) is a key factor (although not, in and of itself, determinative) of construction contract accounting.</p> <p>At the same time, with the aforementioned scope focus on the construction of a single asset or a combination of interrelated or interdependent assets to a buyer's specifications, the construction accounting guidance is generally not applied to the recurring production of goods.</p>

Impact	US GAAP	IFRS
Construction contracts (continued)	<p>Completed-contract method</p> <p>While the percentage-of-completion method is preferred, the completed-contract method is required in certain situations (e.g., inability to make reliable estimates).</p> <p>For circumstances in which reliable estimates cannot be made, but there is an assurance that no loss will be incurred on a contract (e.g., when the scope of the contract is ill defined, but the contractor is protected from an overall loss), the percentage-of-completion method based on a zero-profit margin, rather than the completed-contract method, is recommended until more-precise estimates can be made</p> <p>Percentage-of-completion method</p> <p>Within the percentage-of-completion model there are two acceptable approaches: the revenue approach and the gross-profit approach.</p> <p>Combining and segmenting contracts</p> <p>Combining and segmenting contracts is permitted provided certain criteria are met, but it is not required, so long as the underlying economics of the transaction are fairly reflected.</p>	<p>Completed-contract method</p> <p>The completed-contract method is prohibited.</p> <p>Percentage-of-completion method</p> <p>IFRS utilizes a revenue-approach method of percentage of completion. When the final outcome cannot be estimated reliably, a zero-profit method is utilized (wherein revenue is recognized to the extent of costs incurred if those costs are expected to be recovered). The gross-profit approach is not allowed.</p> <p>Combining and segmenting contracts</p> <p>Combining and segmenting contracts is required when certain criteria are met.</p>

Impact	US GAAP	IFRS
<p>Sale of goods—continuous transfer</p> <p>Outside of construction accounting under IFRS, some agreements for the sale of goods will qualify for revenue recognition by reference to the stage of completion.</p>	<p>Other than construction accounting, US GAAP does not have a separate model equivalent to the continuous transfer notion for sale of goods.</p>	<p>When an agreement is for the sale of goods and is outside the scope of construction accounting, an entity considers whether all of the sale of goods revenue recognition criteria are met continuously as construction progresses. When all of the continuous transfer criteria are achieved, an entity recognizes revenue by reference to the stage of completion using the percentage-of-completion method.</p> <p>The requirements of the construction contracts guidance are generally applicable to the recognition of revenue and the associated expenses for such continuous transfer transactions.</p> <p>Achieving the continuous transfer requirements is expected to be relatively rare in practice.</p>

Impact	US GAAP	IFRS
Barter transactions In certain circumstances the two frameworks require different methods for determining the value ascribed to barter transactions.	<p>Non-advertising-barter transactions The fair value of goods or services received can be used if the value surrendered is not clearly evident.</p> <p>Accounting for advertising-barter transactions If the fair value of assets surrendered in an advertising-barter transaction is not determinable, the transaction should be recorded based on the carrying amount of advertising surrendered, which likely will be zero.</p> <p>Accounting for barter-credit transactions It should be presumed that the fair value of the nonmonetary asset exchanged is more clearly evident than the fair value of the barter credits received. However, it is also presumed that the fair value of the nonmonetary asset does not exceed its carrying amount unless there is persuasive evidence supporting a higher value. In rare instances, the fair value of the barter credits may be utilized (e.g., if the entity can convert the barter credits into cash in the near term, as evidenced by historical practice).</p>	<p>Non-advertising-barter transactions When the fair value of items received is not reliably determinable, the fair value of goods or services surrendered can be used to measure the transaction.</p> <p>Accounting for advertising-barter transactions Revenue from a barter transaction involving advertising cannot be measured reliably at the fair value of advertising services received. However, a seller can reliably measure revenue at the fair value of the advertising services it provides if certain criteria are met.</p> <p>Accounting for barter-credit transactions There is no further/specific guidance for barter-credit transactions. The broader principles outlined/referred to above should be applied.</p>

Impact	US GAAP	IFRS
Extended warranties The IFRS requirement to separately attribute relative fair value to each component of an arrangement has the potential to impact the timing of revenue recognition for arrangements that include a separately priced extended warranty or maintenance contract.	<p>Revenue associated with separately priced extended warranty or product maintenance contracts should generally be deferred and recognized as income on a straight-line basis over the contract life. An exception exists where historical experience indicates that the cost of performing services is incurred on an other-than-straight-line basis.</p> <p>The revenue related to separately priced extended warranties is determined by reference to the selling price for maintenance contracts that are sold separately from the product. There is no relative fair market value allocation in this instance.</p>	<p>If an entity sells an extended warranty, the revenue from the sale of the extended warranty should be deferred and recognized over the period covered by the warranty.</p> <p>In instances where the extended warranty is an integral component of the sale (i.e., bundled into a single transaction), an entity should attribute relative fair value to each component of the bundle.</p>
Discounting of revenues Discounting of revenues (to present value) is more broadly required under IFRS than under US GAAP. This may result in lower revenue under IFRS because the time value portion of the ultimate receivable is recognized as finance/interest income.	<p>The discounting of revenues is required in only limited situations, including receivables with payment terms greater than one year and certain industry-specific situations, such as retail land sales or license agreements for motion pictures or television programs.</p> <p>When discounting is required, the interest component should be computed based on the stated rate of interest in the instrument or a market rate of interest if the stated rate is considered unreasonable.</p>	<p>Discounting of revenues to present value is required in instances where the inflow of cash or cash equivalents is deferred.</p> <p>In such instances, an imputed interest rate should be used for determining the amount of revenue to be recognized as well as the separate interest income component to be recorded over time.</p>
Technical references		
IFRS	IAS 11, IAS 18, IFRIC 13, IFRIC 15, IFRIC 18, SIC 31	
US GAAP	ASC 605-20-25-1 through 25-6, ASC 605-20-25-14 through 25-18, ASC 605-25, ASC 605-35, ASC 605-50, ASC 985-605, CON 5, SAB Topic 13	

Note

The foregoing discussion captures a number of the more significant GAAP differences. It is important to note that the discussion is not inclusive of all GAAP differences in this area.

Recent/proposed guidance**Joint FASB/IASB Discussion Paper: *Preliminary Views on Revenue Recognition in Contracts with Customers***

In December 2008, a joint discussion paper titled *Preliminary Views on Revenue Recognition in Contracts with Customers* was issued. The proposed model outlined in the discussion paper would have a significant impact on current revenue recognition policies under both IFRS and US GAAP. Every industry within the scope of the project may be impacted to some extent. Some entities, particularly those that have historically followed industry-specific guidance, will see pervasive changes. A single contract-based, asset-and-liability model is proposed, where revenue is recognized based on increases in contract assets or decreases in contract liabilities.

A few of the changes under the proposed model are as follows. The percentage-of-completion method historically used for both construction contracts and, where applicable, service arrangements, may no longer exist as a separate model. Rather, revenue in those arrangements will be recognized based on the transfer of control. The definition of a performance obligation may result in separation of more obligations within an arrangement. For example, under current guidance, warranty obligations are recorded as a cost accrual at the time of sale. Such warranties may be a separate performance obligation under the proposed model and would result in revenue deferral as opposed to cost accrual. The increase in identification and separation of performance obligations may also require greater use of estimates than is the case under current practice. Industries where the use of fair value estimates is restricted, such as software accounting under US GAAP which requires VSOE of fair value, will be particularly impacted. Sales-type incentives such as free products or customer loyalty programs are currently recognized as marketing expense in some circumstances. The proposed model requires that those incentives be considered performance obligations and revenue deferred until such obligations are satisfied, as when a customer redeems loyalty points. This change would align US GAAP with the guidance for customer loyalty programs under IFRS.

IFRIC 18: *Transfers of Assets from Customers*

In January 2009, the International Financial Reporting Interpretations Committee (IFRIC) issued IFRIC 18, *Transfers of Assets from Customers*. The interpretation addresses the diversity in practice that arises when entities receive from a customer an item of property, plant and equipment that the entity must then use either to connect the customer to a network or provide the customer with ongoing access to a supply of goods or services, or both. The interpretation also applies to agreements in which an entity receives cash from a customer, and the cash must be used in certain specified manners. The impact of the IFRIC may be relatively broad as it includes guidance around assessing when an entity controls an asset as well as when a component of a revenue transaction should be separately identified and accounted for.

DRAFT EITF 08-1: Revenue Arrangements with Multiple Deliverables

The Emerging Issues Task Force (EITF) recently issued a draft abstract of EITF 08-1, *Revenue Arrangements with Multiple Deliverables*. This Issue will supersede current US GAAP guidance in this area and will become the standard guidance under US GAAP for many multiple-element arrangements. It is currently anticipated that the Issue will require the use of an estimated selling price for the undelivered unit of accounting in transactions in which VSOE or TPE (third-party evidence) of fair value does not exist. The Issue specifies that the estimated selling price shall not exceed the selling price of the delivered unit(s) of accounting based on VSOE or TPE, if known. Given that entities will be required to use an estimated selling price to determine the fair value of an element, the Issue also eliminates the use of the residual method. The first key change—permitting the use of estimated selling prices—will align US GAAP more closely to IFRS on this point. However, EITF 08-1 retains the principle that the amount allocable to a delivered item is limited to the amount that is not contingent on the delivery of additional items. That is, the amount allocable to the delivered item or items is the lesser of the amount otherwise allocable in accordance with the standard or the noncontingent amount. IFRS does not include this requirement. The second key change—eliminating the residual method—will have a significant impact on entities that currently use that method to estimate fair value. This creates a new difference as IFRS permits the residual method. This guidance is expected to be issued in late 2009 and to be effective for new or materially modified arrangements in fiscal years beginning on or after June 15, 2010.

DRAFT EITF 08-9: Milestone Method of Revenue Recognition

The EITF also recently issued a draft abstract of EITF 08-9, *Milestone Method of Revenue Recognition*. This Issue serves to codify a method that has been used in practice to recognize the revenue related to additional contingent consideration in an arrangement. In certain revenue arrangements, such as a collaboration agreement between a large pharmaceutical company and a smaller biotechnology company, early fixed payments from one party to the other for services are supplemented by additional payments that might be made contingent upon the achievement of goals or milestones. Under the milestone method, the additional consideration from achievement of the event (or milestone) is considered indicative of the value provided to the customer through either (a) the vendor's performance or (b) a specific outcome resulting solely or in part from the vendor's performance (for example, performance of research and development services by a biotechnology company that leads to US Food and Drug Administration approval). This Issue defines a milestone as an event for which there is substantial uncertainty at the date the arrangement is entered into that the event will be achieved, when that event can only be achieved based in whole or in part on the vendor's performance or a specific outcome resulting from the vendor's performance, and, if the event is achieved, would result in additional payments being due to the vendor. The Issue specifies that a vendor shall recognize the arrangement consideration that is contingent upon the achievement of a milestone in its entirety in the period in which the milestone is achieved, provided the milestone is substantive.

General

As evidenced by the standards described above, US GAAP and IFRS continue to evolve in the area of revenue recognition. As a further example, the EITF is considering whether to modify the scope of Statement of Position (SoP) 97-2 to exclude certain software-enabled tangible products currently accounted for under SoP 97-2 because they contain software that is "more than incidental." We expect that this evolution will continue.

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Expense recognition

Expense recognition—share-based payments

Despite the progress made by the FASB and the IASB toward converging the frameworks in this area, a multitude of significant differences remain.

The broader scope of share-based payments guidance under IFRS leads to differences associated with awards made to nonemployees, impacting both the measurement date and total value of expense to be recognized.

Differences within the two frameworks may result in differing grant dates and/or different classifications of an award as a component of equity or as a liability. Once an award is classified as a liability, it needs to be remeasured to fair value at each period through earnings, which introduces earnings volatility while also impacting balance sheet metrics and ratios. Certain types of awards (e.g., puttable awards and awards with vesting conditions outside of service, performance or market conditions) are likely to have different equity-versus-liability classification conclusions under the two frameworks.

In addition, companies that issue awards with graded vesting (e.g., awards that vest ratably over time, such as 25 percent per year over a four-year period) may encounter accelerated expense recognition and potentially a different total value to be expensed (for a given award) under IFRS. The impact in this area could lead some companies to consider redesigning the structure of their share-based payment plans. By changing the vesting pattern to cliff vesting (from graded vesting), companies can avoid a front loading of share-based compensation expense, which may be desirable to some organizations.

The deferred income tax accounting requirements for share-based payments vary significantly from US GAAP. Companies can expect to experience greater variability in their effective tax rate over the lifetime of share-based payment awards under IFRS. This variability will be linked with, but move counter to, the issuing company's stock price. For example, as a company's stock price increases, a greater income statement tax benefit will occur, to a point, under IFRS. Once a benefit has been recorded, subsequent decreases to a company's stock price may increase income tax expense within certain limits. The variability is driven by the requirement to remeasure and record through earnings (within certain limits) the deferred tax attributes of share-based payments each reporting period.

Further details on the foregoing and other selected differences are described in the following table.

Impact	US GAAP	IFRS
<p>Scope</p> <p>Some awards categorized as nonemployee instruments under US GAAP will be treated as employee awards under IFRS. The measurement date and expense will be different for awards that are categorized as nonemployee instruments under US GAAP as compared to IFRS.</p> <p>Companies that adopt IFRS will apply a single standard to all share-based payment arrangements, regardless of whether the counterparty is a nonemployee.</p>	<p>The guidance is focused on/driven by the legal definition of an employee with certain specific exceptions/exemptions. ASC 718, <i>Compensation—Stock Compensation</i>, applies to awards granted to employees and Employee Stock Ownership Plans. ASC 505-50 applies to grants to nonemployees.</p>	<p>IFRS focuses on the nature of the services provided and treats awards to employees and others providing employee-type services similarly. Awards for goods from vendors or nonemployee-type services are treated differently. IFRS 2, <i>Share-based payments</i>, includes accounting for all employee and nonemployee arrangements. Furthermore, under IFRS, the definition of an employee is broader than the US GAAP definition.</p>
<p>Measurement of awards granted by nonpublic companies</p> <p>Companies that adopt IFRS will not have alternatives in choosing a measurement method.</p>	<p>Equity-classified</p> <p>The guidance allows nonpublic companies to measure stock-based-compensation awards by using the fair-value (preferred) method or the calculated-value method. If the terms of an award are so complex, a nonpublic company could use the intrinsic-value method.</p> <p>Liability-classified</p> <p>The guidance allows nonpublic companies to make an accounting-policy decision on how to measure stock-based-compensation awards that are classified as liabilities. Such companies may use the fair-value method, calculated-value method, or intrinsic-value method.</p>	<p>IFRS does not include such alternatives for nonpublic companies and requires the use of the fair-value method in all circumstances.</p>

Impact	US GAAP	IFRS
<p>Classification of certain instruments as liabilities or equity</p> <p>Although ASC 718 and IFRS 2 contain a similar principle for classification of stock-based-compensation awards, certain awards will be classified differently under the two standards. In some instances, awards will be classified as equity under US GAAP and a liability under IFRS, while in other instances, awards will be classified as a liability under US GAAP and equity under IFRS.</p>	<p>In certain situations, puttable shares may be classified as equity awards.</p> <p>Liability classification is required when an award is based on a fixed monetary amount settled in a variable number of shares.</p> <p>ASC 718 contains guidance on determining whether to classify an award as equity or a liability. ASC 718 also references the guidance in ASC 480, <i>Distinguishing Liabilities from Equity</i>, when assessing classification of an award.</p>	<p>Puttable shares are always classified as liabilities.</p> <p>Share-settled awards are classified as equity awards even if there is variability in the number of shares due to a fixed monetary value to be achieved.</p> <p>IFRS 2 follows a similar principle of equity/liability classification as ASC 718. However, while IAS 32 has similar guidance to ASC 480, companies applying IFRS 2 are out of the scope of IAS 32. Therefore, equity/liability classification is determined wholly on whether awards are ultimately settled in equity or cash, respectively.</p>
<p>Awards with conditions other than service, performance or market conditions</p> <p>Certain awards classified as liabilities under US GAAP may be classified as equity under IFRS.</p>	<p>If an award contains conditions other than service, performance or market conditions (referred to as "other" conditions), it is classified as a liability award.</p>	<p>If an award of equity instruments contains conditions other than service, performance or market vesting conditions, it is still classified as an equity-settled award.</p> <p>For periods beginning on or after January 1, 2009, such conditions may be non-vesting conditions. Non-vesting conditions are taken into account when determining the grant date fair value of the award.</p>

Impact	US GAAP	IFRS
Service-inception date, grant date, and requisite service <p>Because of the differences in the definitions, there may be differences in the grant date and the time period over which compensation cost is recognized.</p>	<p>The guidance provides specific definitions of service-inception date, grant date, and requisite service, which, when applied, will determine the beginning and end of the period over which compensation cost will be recognized. Additionally, the grant date definition includes a requirement that the employee begins to be affected by the risks and rewards of equity ownership.</p>	<p>IFRS does not include the same detailed definitions or the requirement that the employee begins to be affected by the risks and rewards of equity ownership in the grant date definition.</p>
Attribution—awards with service conditions and graded-vesting features <p>The alternatives included under US GAAP provide for differences in both the measurement and attribution of compensation costs.</p>	<p>Companies are permitted to make an accounting policy election regarding the attribution method for awards with service conditions and graded-vesting features. The choice in attribution method is not linked to the valuation method that the company uses. For awards with graded vesting and performance or market conditions, the graded-vesting attribution approach is required.</p>	<p>Companies are not permitted to choose how the valuation or attribution method is applied to awards with graded-vesting features. Companies should treat each installment of the award as a separate grant. This means that each installment will be separately measured and attributed to expense over the related vesting period.</p>
Tax withholding arrangements—impact to classification <p>There could be a difference in award classification as a result of tax withholding arrangements.</p>	<p>An award containing a net settled tax withholding clause could be equity-classified so long as the arrangement permits tax withholding at the company's minimum statutory rate. If tax withholding is permitted at some higher rate then the whole award would be classified as a liability.</p>	<p>IFRS does not contain a similar exception. Under IFRS, for an award to be wholly classified as equity-settled, the entity should settle the transaction by issuing the gross number of shares under option upon exercise. Conversely, where an employer settles an employee's tax withholding liability using its own cash, the payment is treated as a cash-settled award. The classification of the net balance of the award settled in shares is not affected.</p>

Impact	US GAAP	IFRS
<p>Accounting for income tax effects</p> <p>Companies reporting under IFRS will generally have greater volatility in their deferred tax accounts over the life of the awards due to the related adjustments for stock price movements in each reporting period.</p> <p>Companies reporting under US GAAP could potentially have greater volatility upon exercise arising from the variation between the estimated deferred taxes recognized and the actual tax deductions realized.</p> <p>There are also differences in the presentation of the cash flows associated with an award's tax benefits.</p>	<p>The US GAAP model for accounting for income taxes requires companies to record deferred taxes as compensation cost is recognized. The measurement of the deferred tax asset is based on an estimate of the future tax deduction, if any, for the amount of compensation cost recognized for book purposes. Changes in the stock price do not impact the deferred tax asset or result in any adjustments prior to settlement or expiration. Although they do not impact deferred tax assets, future changes in the stock price will nonetheless affect the actual future tax deduction (if any).</p> <p>Excess tax benefits ("windfalls") upon settlement of an award are recorded in equity. "Shortfalls" are recorded as a reduction of equity to the extent the company has accumulated windfalls in its pool of windfall tax benefits. If the company does not have accumulated windfalls, shortfalls are recorded to income tax expense.</p> <p>In addition, the excess tax benefits upon settlement of an award would be reported as cash inflows from financing activities.</p>	<p>The measurement of the deferred tax asset in each period is based on an estimate of the future tax deduction, if any, for the award measured at the end of each reporting period (based upon the current stock price).</p> <p>When the expected tax benefits from equity awards exceed the recorded cumulative recognized expense multiplied by the tax rate, the tax benefit up to the amount of the tax effect of the cumulative book compensation expense is recorded in the income statement; the excess is recorded in equity.</p> <p>When the expected tax benefit is less than the tax effect of the cumulative amount of recognized expense, the entire tax benefit is recorded in the income statement. IFRS 2 does not include the concept of a pool of windfall tax benefits to offset shortfalls.</p> <p>In addition, all tax benefits or shortfalls upon settlement of an award are generally reported as operating cash flows.</p>

Impact	US GAAP	IFRS
Recognition of social charges (e.g., payroll taxes) The timing of recognition of social charges will generally be earlier under IFRS than US GAAP.	A liability for employee payroll taxes on employee stock-based-compensation should be recognized on the date of the event triggering the measurement and payment of the tax (generally the exercise date for a nonqualified option).	Social charges, such as payroll taxes levied on the employer in connection with stock-based-compensation plans, are expensed in the income statement when the related compensation expense is recognized. The guidance in IFRS for cash-settled share-based payments would be followed in recognizing an expense for such charges.
Valuation—SAB Topic 14 guidance on expected volatility and expected term Companies that report under US GAAP may place greater reliance on implied short-term volatility to estimate volatility. Companies that report under IFRS do not have the option of using the “simplified method” provided by SAB Topic 14. As a result, there may be differences in estimated fair values.	SAB Topic 14 includes guidance on expected volatility and expected term, which includes (1) guidelines for reliance on implied volatility and (2) the “simplified method” for calculating expected term for qualifying awards.	IFRS does not include comparable guidance.
Certain aspects of modification accounting Differences between the two standards for improbable to probable modifications may result in differences in the compensation costs that are recognized.	An “improbable-to-probable” Type III modification can result in recognition of compensation cost that is less than the estimated fair value of the award on the grant date, if expectations about the probability of vesting are accurate. When a modification makes it probable that a vesting condition will be achieved, and the company does not expect the original vesting conditions to be achieved, the grant-date fair value of the award would not be a floor for the amount of compensation cost recognized.	Under IFRS, if the vesting conditions of an award are modified in a manner that is beneficial to the employee, this would be accounted for as a change in only the number of options that are expected to vest (from zero to a new amount of shares), and the award’s full original grant-date fair value would be recognized over the remainder of the service period. That result is the same as if the modified performance condition had been in effect on the grant date.

Impact	US GAAP	IFRS
Employee stock purchase plan (ESPP) ESPPs will be generally deemed compensatory more often under IFRS than under US GAAP.	<p>ESPPs are compensatory if terms of the plan:</p> <ul style="list-style-type: none"> • Either: (a) are more favorable than those available to all shareholders or (b) if the discount from the market price exceeds the percentage of stock issuance costs avoided (discount of 5 percent or less is a safe harbor); • Do not allow all eligible employees to participate on an equitable basis; and • Include any option features (e.g., look backs). 	ESPPs are compensatory. IFRS does not permit any safe-harbor discount for ESPPs nor permit any option features.
Alternative vesting triggers It is likely that awards that become exercisable based on achieving one of several conditions would result in a revised expense recognition pattern (as the awards would be bifurcated under IFRS).	An award that becomes exercisable based on the achievement of either a service condition or a market condition is treated as a single award. Because such an award contained a market condition, compensation cost associated with the award would not be reversed if the requisite service period is met.	An award that becomes exercisable based on the achievement of either a service condition or a market condition is treated as two awards with different service periods, fair values, etc. Any compensation cost associated with the service condition would be reversed if the service was not provided. The compensation cost associated with the market condition would not be reversed.
Cash-settled awards with a performance condition For a cash-settled award where the performance condition is not probable, liability and expense recognition may occur earlier under IFRS.	For cash-settled awards with a performance condition, where the performance condition is not probable, there may be no liability recognized under US GAAP.	For cash settled awards even where the performance condition is not probable (i.e. greater than zero but under 50% probability), a liability is recognized under IFRS based upon the fair value.

Impact	US GAAP	IFRS
Derived service period For an award containing a market condition that is fully vested and deep-out-of-the-money at grant date, expense recognition may occur earlier under IFRS.	US GAAP contains the concept of a derived service period for awards that contain market conditions. Where an award containing a market condition is fully vested and deep-out-of-the-money at grant date but allows employees only a limited amount of time to exercise their awards in the event of termination, US GAAP presumes that employees must provide some period of service to earn the award. Since there is no explicit service period stated in the award, a derived service period must be determined by reference to a valuation technique. The expense for the award would be recognized over the derived service period and reversed if the employee does not complete the requisite service period.	IFRS does not define a derived service period for fully vested, deep-out-of-the-money awards. Therefore, the related expense for such an award would be recognized in full at the grant date since the award is fully vested at that date.
Technical references		
IFRS	IFRS 2, IFRIC 8, IFRIC 11	
US GAAP	ASC 505, ASC 505-50, ASC 718, ASC 815-40, SAB Topic 14-D	

Note

The foregoing discussion captures a number of the more significant GAAP differences. It is important to note that the discussion is not inclusive of all GAAP differences in this area.

Recent/proposed guidance**Amendments to IFRS 2, Group Cash-settled Share-based Payment Transactions**

In June 2009, the IASB issued amendments to IFRS 2 finalizing the proposals in the December 2007 exposure draft on *Group Cash-settled Share-based Payment Transactions*. The amendments clarify the scope and address the accounting for group cash-settled share-based payment transactions in the separate financial statements of the entity receiving the related goods or services when that entity has no obligation to settle the transaction. In such a case, the entity receiving the goods or services would account for the transaction as an equity-settled share-based payment, and the group entity settling the transaction would account for the share-based payment as cash-settled. The amendment also incorporates the guidance in IFRIC 8, *Scope of IFRS 2* and IFRIC 11, *IFRS 2—Group and treasury share transactions*, into IFRS 2, which will result in the withdrawal of these two interpretations.

Under IFRS for the separate financial statements of the subsidiary, the amendment looks to who has the obligation to settle the subsidiary awards to determine equity or liability classification. Under US GAAP, generally push down accounting of the expense recognized at the parent level would apply.

Accordingly, this will lead to differences between US GAAP and IFRS. The amendment is effective for annual periods beginning on or after January 1, 2010. Early adoption is permitted.

Expense recognition—employee benefits

There are a number of significant differences between IFRS and US GAAP in the area of accounting for pension and other post-retirement and postemployment benefits. Some differences will result in less earnings volatility, while others will result in greater earnings volatility. The net effect depends on the individual facts and circumstances for a given company. Further differences could have a significant impact on presentation, operating metrics and key ratios. Note that the IASB and the FASB use the term postemployment differently. The IASB uses the term postemployment to include pension, postretirement, and other postemployment benefits, whereas the FASB uses the term postretirement (OPEB) to include postretirement benefits, other than pensions and other postemployment benefits, and the term postemployment benefits to include benefits before retirement.

A selection of differences is summarized below.

Under IFRS, a company can adopt a policy that would allow recognition of gains/losses in other comprehensive income. Gains/losses treated in accordance with this election would be exempt from being subsequently recorded within the income statement. This election generally reduces the volatility of pension expense recorded within a company's income statement because gains/losses would be recorded only within other comprehensive income. Other policy elections available under IFRS for gain/loss recognition (i.e., corridor approach or immediate recognition within the income statement) are similar to those under US GAAP.

Under IFRS, companies are not required to present the full funded status of their postemployment benefit plans on the balance sheet. However, companies are required to disclose the full funded status within the notes to the financial statements.

US GAAP permits the use of a calculated asset value (to spread market movements over periods of up to five years) in the determination of expected returns on plan assets. IFRS prohibits the use of a calculated value and requires that the actual fair value of plan assets at each measurement date be used.

Under IFRS there is no requirement to present the various components of pension cost as a net amount. As such, companies are permitted to present components of net pension cost within different line items on the income statement. The flexibility provided under IFRS would enable companies to record the interest expense and return on plan assets components of pension expense as part of financing within the income statement.

Differences between US GAAP and IFRS can also result in different classifications of a plan as a defined benefit or a defined contribution plan. It is possible that a benefit arrangement that is classified as a defined contribution plan under US GAAP may be classified as a defined benefit plan under IFRS. It is also possible that a benefit arrangement that is classified as a defined benefit plan under US GAAP may be classified as a defined contribution plan under IFRS. Differences in plan classification could have a significant effect on the expense recognition model and balance sheet presentation.

Both the FASB and the IASB have major projects on their agendas on accounting for pension and other postemployment benefits, which may result in greater convergence in the future. Both boards are expected to decide whether to retain the various deferred recognition and "smoothing" techniques allowed under current guidance, and both are expected to reconsider where the components of benefit cost should be presented separately in the income statement. The IASB is moving faster than the FASB and recently reached tentative conclusions on these matters, as further discussed in the Recent/proposed Guidance section below. The FASB is expected to consider the IASB's conclusions once it begins deliberations on its own project.

Further details on the foregoing and other selected differences are described in the following table.

Impact	US GAAP	IFRS
<p>Expense recognition—actuarial gains/losses</p> <p>Under IFRS, companies can adopt a policy that would allow recognition of gains/losses in other comprehensive income. Gains/losses treated in accordance with such election are not subsequently recorded within profit or loss.</p> <p>Such election would generally reduce the volatility of pension expense in a company's income statement because these gains/losses would be recorded only within other comprehensive income.</p> <p>Note: Gains and losses as referenced under US GAAP include (1) the differences between actual and expected return on assets and (2) changes in the measurement of the benefit obligation. These are similar to actuarial gains and losses referenced under IFRS. Within this publication we have used the term gains and losses when referencing actuarial gains and losses.</p>	<p>The literature permits companies to either (1) record expense for gains/losses in the period incurred within the statement of operations or (2) defer gains/losses through the use of the corridor approach (or any systematic method that results in faster recognition than the corridor approach).</p> <p>Whether gains/losses are recognized immediately or are amortized in a systematic fashion, they are ultimately recorded within the statement of operations as components of net periodic pension expense.</p>	<p>In addition to the choices available under US GAAP, IFRS allows companies to recognize all gains/losses immediately in other comprehensive income. Once recognized in other comprehensive income, actuarial gains/losses are not subsequently recorded within profit or loss.</p>
<p>Income statement classification</p> <p>Under IFRS, companies have the option of disclosing different components of pension/OPEB costs within different line items on the income statement.</p> <p>This could result in companies recording interest cost and expected return on plan assets as part of financing.</p>	<p>All components of net pension/OPEB cost must be aggregated and presented as a net amount in the income statement.</p> <p>While it is appropriate to allocate a portion of net pension expense to different line items (such as cost of goods sold if other employee costs are included in this caption), the disaggregation and separate reporting of different components of net pension expense are precluded.</p>	<p>There is no requirement to present the various components of net pension cost as a single item or a set of items all presented on a net basis within the income statement. Rather, the guidance allows for the potential disaggregation of the component pieces of pension/OPEB cost.</p>

Impact	US GAAP	IFRS
Expense recognition—prior-service costs and credits <p>IFRS has the potential to accelerate expense/credit recognition in income for the effects of plan amendments that create an increase (or decrease) to the benefit obligation (i.e., prior-service cost).</p>	<p>Prior-service cost should be recognized in other comprehensive income at the date of the adoption of the plan amendment and then amortized into income over the participants':</p> <ol style="list-style-type: none"> 1. remaining years of service (for pension plans except where all or almost all plan participants are inactive in terms of not earning additional pension benefits for future service); 2. service to full eligibility date (for other postretirement benefit plans where all or almost all plan participants are inactive in terms of not earning additional pension benefits for future service); or 3. life expectancy (for plans that have all or almost all inactive employees). <p>Negative prior-service cost should be recognized as a prior-service credit to other comprehensive income and used first to reduce any remaining positive prior-service cost included in accumulated other comprehensive income. Any remaining prior-service credits should then be amortized over the remaining service period of the active employees unless all or almost all plan participants are inactive, in which case the amortization period would be the plan participants' life expectancies.</p>	<p>For active employees not yet vested, prior-service cost should be recognized, in income, on a straight-line basis over the period until the benefits become vested.</p> <p>To the extent that the incremental benefits are vested as of the date of the plan amendment, the cost of those benefits should be recognized immediately in the income statement.</p> <p>Negative prior-service cost is accounted for the same as positive prior service costs.</p>

Impact	US GAAP	IFRS
<p>Expected return on plan assets</p> <p>Under IFRS, companies are not permitted to use a calculated value of plan assets (reflecting changes in fair value over a period up to five years) in the determination of expected return on plan assets and in the related accounting for asset gains and losses.</p>	<p>Plan assets should be measured at fair value for balance sheet recognition and for disclosure purposes. However, for the purposes of determination of the expected return on plan assets and the related accounting for asset gains and losses, plan assets can be measured by using either fair value or a calculated value that recognizes changes in fair value over a period of not more than five years.</p>	<p>Plan assets should always be measured at fair value and fair value should be used to determine the expected return on plan assets.</p>
<p>Balance sheet recognition</p> <p>Under IFRS, companies do not present the full funded status of their postemployment benefit plans on the balance sheet. However, companies are required to present the funded status within the footnotes.</p> <p>If, under IFRS, the entity elects to recognize all gains and losses in other comprehensive income or immediately within profit or loss, then generally the only difference with US GAAP on the balance sheet is unrecognized prior service cost.</p>	<p>Entities are required to record on the balance sheet the full funded status (i.e., the differences between the fair value of the plan assets and the projected benefit obligation) of pension plans or the accumulated postretirement benefit obligation of other postretirement plans with the offset to other comprehensive income. This guidance does not have an impact on the recognition of net periodic pension costs.</p>	<p>Entities are required to recognize on the balance sheet the difference between the defined benefit obligation (as defined) and the fair value of plan assets, plus or minus any unrecognized actuarial gains/losses or prior-service costs.</p>

Impact	US GAAP	IFRS	
Substantive commitment to provide pension or other postretirement benefits	Differences in the manner in which a substantive commitment to increase future pension or other postretirement benefits is determined may result in an increased benefit obligation under IFRS.	The determination of whether a substantive commitment exists to provide pension benefits beyond the written terms of a given plan's formula requires careful consideration. Although actions taken by an employer can demonstrate the existence of a substantive commitment, a history of retroactive plan amendments is not sufficient on its own. However, the substantive plan in another postretirement benefit plan should be the basis for determining the obligation.	In certain circumstances, a history of regular increases may indicate: <ol style="list-style-type: none"> 1. a present commitment to make future plan amendments, and 2. that additional benefits will accrue to prior service periods. In such cases, a constructive obligation (to increase benefits) is the basis for determination of the obligation.
Defined benefit versus defined contribution plan classification	Certain plans currently accounted for as defined benefit plans under US GAAP may be accounted for as defined contribution plans under IFRS and vice versa. Classification differences would result in changes to the expense recognition model as well as to balance sheet presentation.	A defined contribution plan is any arrangement that provides benefits in return for services rendered, that establishes an individual account for each participant, and that specifies how recurring periodic contributions to the individual's account should be determined. Multiemployer plans are treated similarly to defined contribution plans.	An arrangement qualifies as a defined contribution plan if a company's legal or constructive obligation is limited to the amount it contributes to a separate entity (generally, a fund or an insurance company). There is no requirement for individual participant accounts. For multiemployer plans, the accounting treatment used is based on the substance of the terms of the plan. If the plan is a defined benefit plan in substance, it should be accounted for as such. However, defined benefit accounting may not be required if the entity does not have sufficient information.

Impact	US GAAP	IFRS
<p>Curtailments</p> <p>A multitude of differences exist in relation to how curtailments are defined, how both curtailment gains and losses are calculated, and when such gains should be recorded. Losses are typically recorded in the same period.</p> <p>When a curtailment is caused by a plan amendment (e.g., a plan freeze), the timing of recognizing a gain or loss is the same under US GAAP or IFRS.</p>	<p>A curtailment is defined as an event that significantly reduces the expected years of future service of present employees or eliminates for a significant number of employees the accrual of defined benefits for some or all of their future service.</p> <p>Curtailment gains are recognized when realized (i.e., once the terminations have occurred).</p> <p>The guidance permits certain offsets of unamortized gains/losses but does not permit pro rata recognition of remaining unamortized gains/losses in a curtailment.</p>	<p>The definition of a curtailment also captures situations where current employees will qualify only for significantly <i>reduced</i> (not necessarily eliminated) benefits.</p> <p>Curtailment gains should be recorded when the entity is demonstrably committed to making a material reduction (as opposed to once the terminations have occurred).</p> <p>IFRS requires the curtailment gain/loss to include a pro rata share of unamortized gains/losses if they are related.</p>
<p>Asset ceiling</p> <p>Under IFRS there is a limitation on the value of the net pension asset that can be recorded on the balance sheet.</p>	<p>There is no limitation on the size of the net pension asset that can be recorded on the balance sheet.</p>	<p>Under the guidance, an asset ceiling test limits the amount of the net pension asset that can be recognized to the lower of (1) the amount of the net pension asset or (2) the sum of any cumulative unrecognized net losses, unrecognized prior-service cost, and the present value of any economic benefits available in the form of refunds or reductions in future contributions to the plan. The guidance also governs the treatment and disclosure of amounts, if any, in excess of the asset ceiling.</p>

Impact	US GAAP	IFRS
<p>Deferred compensation arrangements—employment benefits</p> <p>The accounting for these arrangements, which include individual senior executive employment arrangements, varies under the two frameworks. IFRS provides less flexibility than is available under US GAAP with respect to the expense attribution methodology.</p>	<p>Deferred compensation liabilities are measured at the present value of the benefits expected to be provided in exchange for an employee's service to date. If expected benefits are attributed to more than an individual year of service, the costs should be accrued in a systematic and rational manner over the relevant years of service in which the employee earns the right to the benefit (to the full eligibility date).</p> <p>A number of acceptable attribution models are used in practice. Examples include the sinking-fund model and the straight-line model. Gains and losses are recognized immediately in the income statement.</p>	<p>IFRS does not distinguish between individual senior executive employment arrangements and a “plan” in the way that US GAAP does. Whether a postemployment benefit is provided for one employee or all employees the accounting is the same. Deferred compensation accounting under IFRS relates to benefits that are normally paid while in service but more than 12 months after the end of the accounting period in which they are earned.</p> <p>The liability associated with deferred compensation contracts classified as other long-term benefits under IAS 19 is measured by the projected-unit-credit method (similar to postemployment benefits), with the exception that all prior-service costs and gains and losses are recognized immediately in the income statement.</p> <p>Individual senior executive employment arrangements, classified as post-employment benefits under IAS 19, are accounted for in the same way as post-employment benefit plans.</p>

Impact	US GAAP	IFRS
<p>Plan asset valuation</p> <p>There are differences in the determination of fair value of plan assets under each framework.</p>	<p>Plan assets should be measured at fair value less cost to sell. Fair value should reflect an exit price at which the asset could be sold to another party.</p> <p>For markets in which dealer-based pricing exists, the price that is most representative of fair value—regardless of where it falls on the fair value hierarchy—should be used. As a practical expedient, the use of midmarket pricing is permitted.</p>	<p>Plan assets should always be measured at fair value, which is defined as the amount for which an asset could be exchanged in an arm's-length transaction between knowledgeable and willing parties.</p> <p>For securities quoted in an active market, the bid price should be used.</p>
<p>Discount rates</p> <p>Differences in the selection criteria for discount rates could lead companies to establish different discount rates under IFRS.</p>	<p>The discount rate is based on the rate at which the pension obligation could be effectively settled. Companies may look to the rate of return on high-quality, fixed-income investments with similar durations to those of the benefit obligation, to establish the discount rate. The SEC has stated that the term high-quality means that a bond has received one of the two highest ratings given by a recognized ratings agency (e.g., Aa or higher by Moody's).</p> <p>The guidance does not specifically address circumstances in which a deep market in high-quality corporate bonds does not exist. However, in practice, a hypothetical high-quality bond yield is determined based on a spread added to representative government bond yields.</p>	<p>The discount rate should be determined by reference to market yields on high-quality corporate bonds with durations that are similar to those of the benefit obligation.</p> <p>Where a deep market of high-quality corporate bonds does not exist, companies are required to look to the yield on government bonds when selecting the discount rate.</p>

Impact	US GAAP	IFRS
Accounting for termination indemnities and unfunded defined contribution plans US GAAP allows for more options in accounting for nonqualifying excess 401(k) plans than IFRS, and for non-US termination indemnity programs.	When accounting for termination indemnities and nonqualifying excess 401(k) plans (i.e., unfunded defined contribution plans), there are two acceptable alternatives to account for the obligation under US GAAP: (1) full defined benefit plan accounting, or (2) mark-to-market accounting (i.e. basing the liability on the employee's current account balance).	Defined benefit accounting is required for termination indemnities and nonqualifying excess 401(k) plans. Gains and losses are recognized following the entity's accounting policy for its other defined benefit plans.
Technical references		
IFRS IAS 19, IAS 37, IAS 39, IFRIC 14		
US GAAP ASC 710, ASC 712, ASC 715, ASC 715-30-35-40, ASC 715-20-S55, ASC 715-20-S99, ASC 820, ASC 835-30		

Note

The foregoing discussion captures a number of the more significant GAAP differences. It is important to note that the discussion is not inclusive of all GAAP differences in this area.

Recent/proposed guidance

Employers' Disclosures about Postretirement Benefit Plan Assets

In December 2008, the FASB issued guidance which requires additional disclosures for fiscal years ending after December 15, 2009, with regards to: (1) how investment allocation decisions are made by management, (2) major categories of plan assets, and (3) significant concentrations of risk. Additionally, the FSP requires an employer to disclose information about the valuation of plan assets similar to that required under ASC 820, *Fair Value Measurements and Disclosures*. Those disclosures include: (1) the level within the fair value hierarchy of plan assets, (2) information about the inputs and valuation techniques used to measure the fair value of plan assets, and (3) a reconciliation of the beginning and ending balances of plan assets valued using significant unobservable inputs (Level 3 under ASC 820). The FSP disclosure requirements are more extensive than those currently required under IAS 19. However, as discussed in the Recent/proposed Guidance section of the chapter on Financial Assets, the IASB has issued an exposure draft on fair value measurements. The exposure draft, if approved in its current form, would generally align the plan assets disclosure requirements under IFRS with those required by the new US GAAP standard.

IFRIC 14: IAS (International Accounting Standard) 19—The Limit on a Defined Benefit Asset, Minimum Funding Requirements and Their Interaction

In May 2009, the IASB published an exposure draft proposing amendments to IFRIC 14, *IAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction*. The proposed amendment is aimed at correcting an unintended consequence of IFRIC 14. Under the current guidance, some entities are not permitted to recognize certain prepayments for minimum funding contributions as an asset. The proposals will remedy this by requiring prepayments to be recognized as assets in certain circumstances. A 60-day comment period ended July 27, 2009. Differences to US GAAP will remain as IFRS will retain certain limitations on defined benefit assets, whereas US GAAP has no such limitations.

Preliminary Views on Amendments to IAS 19, Employee Benefits

In March 2008 the IASB issued a discussion paper on employee benefits. Comments on the discussion paper were due in September 2008. In April 2009, the IASB completed its deliberations for the recognition and presentation of pension and other postretirement obligations that will lead to an exposure draft of new guidance. The Board tentatively decided that entities should recognize all changes in the value of plan assets and in the obligation in the financial statements in the period in which they occur. The Board also tentatively decided that entities should recognize in the income statement unvested prior service cost in the period of a plan amendment. With these two decisions, the Board would eliminate the deferred recognition methods for gains and losses, including the corridor method, and deferred recognition of prior service cost. Additionally, the Board tentatively decided to separate the components of pension/OPEB expense between an employment component (included in the operating section of the income statement and would consist of service cost and prior service cost arising from plan amendments, and changes in the obligation due to a plan curtailment), a financing component (included in the financing section of the income statement and would consist of interest cost), and a remeasurement component (presented on a net of tax basis and would consist of gains and losses on the obligation as well as the actual change in the fair value of plan assets, gains and losses related to settlements, and the asset ceiling adjustments). The IASB plans to release an exposure draft in the fourth quarter of 2009. After another round of deliberations, the IASB intends to issue a final standard in 2011 with an effective date of January 1, 2013.

The IASB also recently deliberated the rate at which a post-employment benefit obligation should be discounted. Currently, IAS 19 requires the discount rate to be determined by reference to market yields on high quality corporate bonds. In situations where a deep market does not exist for such bonds, the market yields on government bonds are required to be used. The Board is discussing whether to remove the requirements to use a government bond rate when there is no deep market in high quality corporate bonds. The Board is working towards issuing an exposure draft in August 2009, with a final standard to be issued by the end of 2009.

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Assets

Assets—nonfinancial assets

The guidance under US GAAP and IFRS as it relates to nonfinancial assets (e.g., intangibles; property, plant and equipment—including leased assets; inventory; and investment property) contains some significant differences that have potentially far-reaching implications.

As it relates to the fundamental carrying basis of nonfinancial assets, IFRS permits the revaluation of certain nonfinancial assets to fair market value, whereas US GAAP generally does not.

Differences in the testing for the potential impairment of long-lived assets held for use may lead to earlier impairment recognition under IFRS. IFRS requires the use of entity-specific discounted cash flows or a fair value measure in tests for the recoverability of an asset. By comparison, US GAAP uses a two-step model that begins with undiscounted cash flows. This fundamental distinction between the impairment models can make the difference between an asset being impaired or not. Additional differences exist, such as what qualifies as an impairment indicator or how recoveries in previously impaired assets are treated.

The recognition and measurement of intangible assets could differ significantly under IFRS. With very limited exceptions, US GAAP prohibits the capitalization of development costs, whereas development costs under IFRS are capitalized if certain criteria are met. Even where US GAAP allows for the capitalization of development costs (e.g., software development costs), differences exist. In the area of software development costs, US GAAP provides different guidance depending on whether the software is for internal use or for sale. The principles surrounding capitalization under IFRS, by comparison, are the same whether the internally generated intangible is being developed for internal use or for sale.

The level at which indefinite lived intangible assets are tested for impairment may vary significantly under the two frameworks. When identifying a unit of account under US GAAP, indefinite-lived intangible assets shall only be grouped with other indefinite-lived intangible assets—those assets cannot be tested in combination with goodwill or with a finite-lived asset. Under IFRS the impairment test will likely be performed at the cash generating unit (CGU) level.

In the area of inventory, IFRS prohibits the use of the last in, first out (LIFO) costing methodology, which is an allowable option under US GAAP. As a result, a company that adopts IFRS and that utilizes the LIFO method would have to move to an allowable costing methodology, such as first-in, first-out or weighted-average cost. For US-based operations, differences in costing methodologies could have a significant impact on reported operating results as well as on current income taxes payable, given the Internal Revenue Service (IRS) book/tax LIFO conformity rules.

IFRS provides criteria for lease classification that are similar to US GAAP criteria. However, the IFRS criteria do not override the basic principle that classification is based on whether the lease transfers substantially all of the risks and rewards of ownership to the lessee. This could result in varying lease classifications for similar leases under the two frameworks. Other key differences involve such areas as sale-leaseback accounting, leveraged leases and real estate transactions.

As further discussed in the Recent/proposed Guidance section below, the IASB and FASB are carrying out a joint project with the objective of comprehensively reconsidering the lease accounting guidance under both frameworks.

Spin-off transactions can result in significantly different income statement implications under the two frameworks. US GAAP accounts for spin-off transactions based on the carrying value of the nonmonetary assets, with the distributions recorded against owner's equity and no gain/loss recorded in income (assuming that the assets were not impaired prior to the spin-off transaction). IFRS requires that dividends payable be recorded at the fair value of the nonmonetary assets to be distributed. Upon settlement, the difference between the carrying value of the dividend payable and the carrying amount of the nonmonetary assets, if any, is recorded in the income statement.

Further details on the foregoing and other selected differences are described in the following table.

Impact	US GAAP	IFRS
General		
<p>Impairment of long-lived assets held for use</p> <p>The IFRS-based impairment model may lead to the need to recognize impairments of long-lived assets held for use earlier than would be required under US GAAP.</p> <p>There are also differences related to such matters as what qualifies as an impairment indicator and how recoveries in previously impaired assets get treated.</p>	<p>US GAAP requires a two-step impairment test and measurement model as follows:</p> <ol style="list-style-type: none"> 1. The carrying amount is first compared with the undiscounted cash flows. If the carrying amount is lower than the undiscounted cash flows, no impairment loss is recognized, although it may be necessary to review depreciation (or amortization) estimates and methods for the related asset. 2. If the carrying amount is higher than the undiscounted cash flows, an impairment loss is measured as the difference between the carrying amount and fair value. Fair value is defined as the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date (an “exit price”). As a result, consideration must be given to the following during step two of an impairment test: <p>Use of Market Participant Assumptions—US GAAP emphasizes that a fair value measurement should be based on the assumptions of market participants and not those of the reporting entity. Therefore, entity-specific intentions should not impact the measurement of fair value unless those assumptions are consistent with market participant views.</p>	<p>IFRS uses a one-step impairment test. The carrying amount of an asset is compared with the recoverable amount. The recoverable amount is the higher of (1) the asset’s fair value less costs to sell or (2) the asset’s value in use.</p> <p>In practice, individual assets do not usually meet the definition of a cash generating unit. As a result, assets are rarely tested for impairment individually but are tested within a group of assets.</p> <p>Fair value less cost to sell represents the amount obtainable from the sale of an asset or cash-generating unit in an arm’s-length transaction between knowledgeable, willing parties less the costs of disposal. The IFRS reference to knowledgeable, willing parties is generally viewed as being consistent with the market participant assumptions noted under US GAAP.</p> <p>IFRS does not contain guidance about which market should be used as a basis for measuring fair value when more than one market exists.</p> <p>Value in use represents the future cash flows discounted to present value by using a pretax, market-determined rate that reflects the current assessment of the time value of money and the risks specific to the asset for which the cash flow estimates have not been adjusted.</p>

Impact	US GAAP	IFRS
Impairment of long-lived assets held for use (continued)	<p>Determining the Appropriate Market— A reporting entity is required to identify and evaluate the markets into which an asset may be sold or a liability transferred. In establishing fair value, a reporting entity must determine whether there is a principal market or, in its absence, a most advantageous market. However, in measuring the fair value of nonfinancial assets and liabilities, in many cases, there will not be observable data or a reference market. As a result, management will have to develop a hypothetical market for the asset or liability.</p> <p>Application of Valuation Techniques— The calculation of fair value will no longer default to a present value technique. While present value techniques may be appropriate, the reporting entity must also consider all valuation techniques appropriate in the circumstances.</p> <p>If the asset is recoverable based on undiscounted cash flows, the discounting or fair value type determinations are not applicable. Changes in market interest rates are not considered impairment indicators.</p> <p>The reversal of impairments is prohibited.</p>	<p>The use of entity-specific discounted cash flows is required in the value in use analysis. Changes in market interest rates can potentially trigger impairment and hence are impairment indicators.</p> <p>If certain criteria are met, the reversal of impairments, other than those of goodwill, is permitted.</p> <p>For noncurrent, nonfinancial assets (excluding investment properties) carried at revalued amounts instead of depreciated cost, impairment losses related to the revaluation are recorded directly in equity to the extent of prior upward revaluations with any further losses being reflected in the income statement.</p>

Impact	US GAAP	IFRS
<p>Cash flow estimates</p> <p>As noted above, impairment testing under US GAAP starts with undiscounted cash flows whereas it starts with discounted cash flows under IFRS. Aside from that difference, IFRS is more prescriptive with respect to how the cash flows themselves are identified for purposes of calculating value in use.</p>	<p>Future cash flow estimates used in an impairment analysis should include:</p> <ul style="list-style-type: none"> • All cash inflows expected from the use of the long-lived asset (asset group) over its remaining useful life, based on its existing service potential; • Any cash outflows necessary to obtain those cash inflows, including future expenditures to maintain (but not improve) the long-lived asset (asset group); and • Cash flows associated with the eventual disposition, including selling costs, of the long-lived asset (asset group). 	<p>Cash flow estimates used to calculate value in use under IFRS should include:</p> <ul style="list-style-type: none"> • Cash inflows from the continuing use of the asset or the activities of the CGU • Cash outflows necessarily incurred to generate the cash inflows from continuing use of the asset or CGU (including cash outflows to prepare the asset for use) and that are directly attributable to the asset or CGU • Cash outflows that are indirectly attributable (such as those relating to central overheads), but that can be allocated on a reasonable and consistent basis to the asset or CGU • Cash flows expected to be received (or paid) for the disposal of assets or CGUs at the end of their useful lives • Cash outflows to maintain the operating capacity of existing assets, including, for example, cash flows for day-to-day servicing

Impact	US GAAP	IFRS
Cash flow estimates (continued)	<p>US GAAP specifies that the remaining useful life of a group of assets over which cash flows can be considered should be based on the remaining useful life of the “primary” asset of the group.</p> <p>Cash flows are from the perspective of the entity itself. Expected future cash flows should represent management’s best estimate and should be based on reasonable and supportable assumptions that are consistent with other assumptions made in the preparation of the financial statements and other information used by the entity for comparable periods.</p>	<p>Cash flow projections used to measure value in use should be based on reasonable and supportable assumptions of the set of economic conditions that will exist over the asset’s remaining useful life.</p> <p>Cash flows expected to arise from future restructurings or from improving the asset’s performance should be excluded.</p> <p>Cash flows are from the perspective of the entity itself.</p> <p>Projections based on management’s budgets/forecasts shall cover a maximum period of five years, unless a longer period can be justified.</p> <p>Estimates of cash flow projections beyond the period covered by the most recent budgets/forecasts should extrapolate the projections based on the budgets/forecasts using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified. This growth rate shall not exceed the long-term average growth rate for the products, industries, or country in which the entity operates, or for the market in which the asset is used.</p>

Impact	US GAAP	IFRS
Asset groupings Determination of asset groupings is a matter of judgment and could result in differences between IFRS and US GAAP	<p>For purposes of recognition and measurement of an impairment loss, a long-lived asset or asset group should represent the lowest level for which an entity can separately identify cash flows that are largely independent of the cash flows of other assets and liabilities.</p> <p>In limited circumstances, a long-lived asset may not have identifiable cash flows that are largely independent of the cash flows of other assets and liabilities and of other asset groups. In those circumstances, the asset group for that long-lived asset shall include all assets and liabilities of the entity.</p>	A cash-generating unit is the smallest group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. It can be a single asset. Identification of an entity's cash-generating units involves judgment. If an active market exists for the output produced by an asset or group of assets, that asset or group should be identified as a cash generating unit, even if some or all of the output is used internally.
Carrying basis The ability to revalue assets (to fair market value) under IFRS may create significant differences in the carrying value of assets as compared with US GAAP.	US GAAP generally utilizes historical cost and prohibits revaluations except for certain categories of financial instruments, which are carried at fair value.	<p>Historical cost is the primary basis of accounting. However, IFRS permits the revaluation to fair value of some intangible assets; property, plant and equipment; and investment property and inventories in certain industries (e.g., commodity broker/dealer).</p> <p>IFRS also requires that biological assets and certain categories of financial instruments be reported at fair value.</p>

Impact	US GAAP	IFRS
Intangible assets		
<p>Internally developed intangibles</p> <p>US GAAP prohibits, with very limited exceptions, the capitalization of development costs. Development costs are capitalized under IFRS if certain criteria are met.</p> <p>Further differences may exist in such areas as software development costs, where US GAAP provides specific detailed guidance depending on whether the software is for internal use or for sale. The principles surrounding capitalization under IFRS, by comparison, are the same, whether the internally generated intangible is being developed for internal use or for sale.</p>	<p>In general, both research costs and development costs are expensed as incurred, making the recognition of internally generated intangible assets rare. However, separate, specific rules apply in certain areas. For example, there is distinct guidance governing the treatment of costs associated with the development of software for sale to third parties. Separate guidance governs the treatment of costs associated with the development of software for internal use. The guidance for the two types of software varies in a number of significant ways. There are, for example, different thresholds for when capitalization commences, and there are also different parameters for what types of costs are permitted to be capitalized.</p>	<p>Costs associated with the creation of intangible assets are classified into research phase costs and development phase costs. Costs in the research phase are always expensed. Costs in the development phase are capitalized if all of the following six criteria are demonstrated:</p> <ul style="list-style-type: none"> • The technical feasibility of completing the intangible asset • The intention to complete the intangible asset • The ability to use or sell the intangible asset • How the intangible asset will generate future economic benefits (the entity should demonstrate the existence of a market or, if for internal use, the usefulness of the intangible asset) • The availability of adequate resources to complete the development • The ability to measure reliably the expenditure attributable to the intangible asset during its development <p>Expenditures on internally generated brands, mastheads, publishing titles, customer lists and items similar in substance cannot be distinguished from the cost of developing the business as a whole. Therefore, such items are not recognized as intangible assets.</p> <p>Development costs initially recognized as expenses cannot be capitalized in a subsequent period.</p>

Impact	US GAAP	IFRS
Indefinite-lived intangible assets—level of assessment for impairment testing <p>Under US GAAP the assessment is performed at the asset level. Under IFRS the assessment may be performed at a higher level (i.e., the cash generating unit level).</p>	<p>Separately recorded indefinite-lived intangible assets, whether acquired or internally developed, shall be combined into a single unit of accounting for purposes of testing impairment if they are operated as a single asset and, as such, are essentially inseparable from one another.</p> <p>Indefinite-lived intangible assets may only be combined with other indefinite-lived intangible assets—they cannot be tested in combination with goodwill or with a finite-lived asset.</p> <p>US GAAP literature provides a number of indicators that an entity should consider in making a determination of whether to combine intangible assets.</p>	<p>As most indefinite-lived intangible assets (e.g., brand name) do not generate cash flows independently of other assets – it may not be possible to calculate the value in use for such an asset on a stand-alone basis. Therefore, it is necessary to determine the smallest identifiable group of assets that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets, known as a cash generating unit, in order to complete the test.</p>
Impairments of software costs to be sold, leased or otherwise marketed <p>Impairments may be recognized sooner under IFRS. Furthermore, when impairments are recognized they will generally be for larger amounts under IFRS.</p>	<p>When assessing potential impairment, the unamortized capitalized costs of a computer software product shall be compared to the net realizable value of that product. The amount by which the unamortized capitalized costs of a computer software product exceed the net realizable value of that asset shall be written off. The net realizable value is the estimated future gross revenue from that product reduced by the estimated future costs of completing and disposing of that product.</p> <p>The net realizable value calculation does not utilize discounted cash flows.</p>	<p>Under IFRS, intangible assets not yet available for use are tested annually for impairment.</p> <p>The higher of either 1) fair value less costs to sell, or 2) value in use are used to determine the recoverable amount, which is then compared to the carrying amount. The value in use calculation uses the present value of future cash flows.</p>

Impact	US GAAP	IFRS
<p>Advertising costs</p> <p>Under IFRS, advertising costs may need to be expensed sooner.</p>	<p>The costs of other than direct response advertising should be either expensed as incurred or deferred and then expensed the first time the advertising takes place. This is an accounting policy decision and should be applied consistently to similar types of advertising activities.</p> <p>Certain direct response advertising costs are eligible for capitalization if, among other requirements, probable future economic benefits exist. Direct response advertising costs that have been capitalized are then amortized over the period of future benefits (subject to impairment considerations).</p> <p>Aside from direct response advertising-related costs, sales materials, such as brochures and catalogues, may be accounted for as prepaid supplies until they no longer are owned or expected to be used, in which case their cost would be a cost of advertising.</p>	<p>Costs of advertising are expensed as incurred. The guidance does not provide for deferrals until the first time the advertising takes place, nor is there an exception related to the capitalization of direct response advertising costs or programs.</p> <p>Prepayment for advertising may be recorded as an asset only when payment for the goods or services is made in advance of the entity's having the right to access the goods or receive the services.</p> <p>The cost of materials, such as sales brochures and catalogues, is recognized as an expense when the entity has the right to access those goods.</p>

Impact	US GAAP	IFRS
Property, plant and equipment		
Asset retirement obligations	<p>IFRS results in greater income statement volatility, as in subsequent periods obligations get adjusted and accreted based on current market-based discount rates.</p> <p>Asset retirement obligations (AROs) are recorded at fair value, and are based upon the legal obligation that arises as a result of an acquisition, construction, or development of a long-lived asset.</p> <p>The use of a credit-adjusted, risk-free rate is required for discounting purposes when an expected present-value technique is used for estimating the fair value of the liability.</p> <p>The guidance also requires an entity to measure changes in the liability for an ARO due to passage of time by applying an interest method of allocation to the amount of the liability at the beginning of the period. The interest rate used for measuring that change would be the credit-adjusted, risk-free rate that existed when the liability, or portion thereof, was initially measured.</p> <p>In addition, changes to the undiscounted cash flows are recognized as an increase or a decrease in both the liability for an ARO and the related asset retirement cost. Upward revisions are discounted by using the current credit-adjusted, risk-free rate. Downward revisions are discounted by using the credit-adjusted, risk-free rate that existed when the original liability was recognized. If an entity cannot identify the prior period to which the downward revision relates, it may use a weighted-average, credit-adjusted, risk-free rate to discount the downward revision to estimated future cash flows.</p>	<p>IFRS requires that management's best estimate of the costs of dismantling and removing the item or restoring the site on which it is located be recorded when an obligation exists. The estimate is to be based on a present obligation (legal or constructive) that arises as a result of the acquisition, construction or development of a long-lived asset. If it is not clear whether a present obligation exists, the entity may evaluate the evidence under a more-likely-than-not threshold. This threshold is evaluated in relation to the likelihood of settling the obligation.</p> <p>The guidance uses a pretax discount rate that reflects current market assessments of the time value of money and the risks specific to the liability.</p> <p>Changes in the measurement of an existing decommissioning, restoration or similar liability that result from changes in the estimated timing or amount of the cash outflows or other resources or a change in the discount rate adjust the carrying value of the related asset under the cost model. Adjustments may not increase the carrying amount of an asset beyond its recoverable amount or reduce it to a negative value. The periodic unwinding of the discount is recognized in profit or loss as a finance cost as it occurs.</p>

Impact	US GAAP	IFRS
Depreciation	<p>Under IFRS, differences in asset componentization guidance may result in the need to track and account for property, plant and equipment at a more disaggregated level. Greater disaggregation may in turn trigger earlier disposal or retirement activity when portions of a larger asset group are replaced.</p>	<p>US GAAP generally does not require the component approach for depreciation. While it would generally be expected that the appropriateness of significant assumptions within the financial statements would be reassessed each reporting period, there is no requirement for an annual review of residual values.</p> <p>IFRS requires that separate significant components of an item of property, plant and equipment with different lives be recorded and depreciated separately. Consistent with the componentization model, the guidance requires that the carrying amount of parts or components that are replaced be derecognized.</p> <p>The guidance includes a requirement to review residual values and useful life at each balance sheet date.</p>
Borrowing costs	<p>US GAAP allows for more judgment in the determination of the capitalization rate that could lead to differences in the amount of costs capitalized.</p> <p>IFRS does not permit the capitalization of borrowing costs in relation to equity-method investments, whereas US GAAP may allow capitalization in certain circumstances.</p>	<p>Capitalization of interest costs while a qualifying asset is being prepared for its intended use is required.</p> <p>The guidance does not require that all borrowings be included in the determination of a weighted-average capitalization rate. Instead, the requirement is to capitalize a reasonable measure of cost for financing the asset's acquisition in terms of the interest cost incurred that otherwise could have been avoided.</p> <p>An investment accounted for by using the equity method meets the criteria for a qualifying asset while the investee has activities in progress necessary to commence its planned principal operations, provided that the investee's activities include the use of funds to acquire qualifying assets for its operations.</p> <p>Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are required to be capitalized as part of the cost of that asset.</p> <p>The guidance acknowledges that determining the amount of borrowing costs that are directly attributable to an otherwise qualifying asset may require professional judgment. Having said that, the guidance first requires the consideration of any specific borrowings and then requires consideration of all general borrowings outstanding.</p> <p>In broad terms, a qualifying asset is one that necessarily takes a substantial period of time to get ready for its intended use or sale. Investments accounted for under the equity method would not meet the criteria for a qualifying asset.</p>

Impact	US GAAP	IFRS
Leases		
Lease classification—general	<p>Leases may be classified differently under IFRS than under US GAAP. Different classification can have a profound effect on how a lease is reflected within the financial statements.</p> <p>The guidance contains four specific criteria for determining whether a lease should be classified as an operating lease or a capital lease by a lessee. The criteria for capital lease classification broadly address the following matters:</p> <ul style="list-style-type: none"> • Ownership transfer of the property to the lessee • Bargain purchase option • Lease term in relation to economic life of the asset • Present value of minimum lease payments in relation to fair value of the leased asset <p>The criteria contain certain specific quantified thresholds such as whether the present value of the minimum lease payments equals or exceeds 90 percent of the fair value of the leased property.</p> <p>For a lessor to classify a lease as a direct financing or sales-type lease under the guidance, two additional criteria must be met.</p>	<p>The guidance focuses on the overall substance of the transaction. Lease classification as an operating lease or a finance lease (i.e., the equivalent of a capital lease under US GAAP) depends on whether the lease transfers substantially all of the risks and rewards of ownership to the lessee.</p> <p>While the lease classification criteria identified in US GAAP are considered in classification of a lease under IFRS, there are no quantitative breakpoints or bright lines to apply (e.g., 90%).</p> <p>A lease of special purpose assets that only the lessee can use without major modification would generally be classified as a finance lease. This would also be the case for any lease where the lessor is not subject to significant risk with respect to the residual value of the leased property.</p> <p>Importantly, there are no incremental criteria for a lessor to consider in classifying a lease under IFRS. Accordingly, lease classification by the lessor and the lessee should typically be symmetrical.</p>

Impact	US GAAP	IFRS
Sale-leaseback arrangements Differences in the frameworks may lead to differences in the timing of gain recognition in sale-leaseback transactions. Where differences exist, IFRS may lead to earlier gain recognition.	<p>The gain on a sale-leaseback transaction is generally deferred and amortized over the lease term. Immediate recognition of the full gain is normally appropriate only when the leaseback is minor, as defined.</p> <p>If the leaseback is more than minor, but less than substantially all of the asset life, a gain is recognized immediately to the extent that the gain exceeds the present value of the minimum lease payments.</p> <p>If the lessee provides a residual value guarantee, the gain corresponding to the gross amount of the guarantee is deferred until the end of the lease; such amount is not amortized during the lease term.</p> <p>When a sale-leaseback transaction results in a capital lease, the gain is amortized in proportion to the amortization of the leased asset.</p> <p>There are onerous rules for determining when sale-leaseback accounting is appropriate for transactions involving real estate. If the rules are not met, the sale leaseback will be accounted for as a financing. As such, the real estate will remain on the seller-lessee's balance sheet and the sales proceeds will be reflected as debt. Thereafter, the property will continue to be depreciated and the rent payments will be recharacterized as debt service.</p>	<p>When a sale-leaseback transaction results in a lease classified as an operating lease, the full gain on the sale would normally be recognized if the sale was executed at the fair value of the asset. It is not necessary for the leaseback to be minor.</p> <p>If the sale price is below fair value, any profit or loss should be recognized immediately, except that if the below-market sale price is compensated for by future lease payments at below-market rates, the impact thereof should be deferred and amortized in proportion to the lease payments over the lease period. If the sale price is above fair value, the excess over fair value should be deferred and amortized over the period for which the asset is expected to be used.</p> <p>When a sale-leaseback transaction results in a finance lease, the gain is amortized over the lease term irrespective of whether the lessee will reacquire the leased property.</p> <p>There are no real estate specific rules equivalent to the US guidance. Accordingly, almost all sale-leaseback transactions result in sale-leaseback accounting. The property sold would be removed from the balance sheet and if the leaseback is classified as an operating lease, the property would not come back onto the seller-lessee's balance sheet.</p>

Impact	US GAAP	IFRS
<p>Leases involving land and buildings</p> <p>More frequent bifurcation under IFRS may result in differences in the classification of and accounting for leases involving land and buildings. In addition, accounting for land leases under IFRS may more frequently result in the recording of a finance lease.</p>	<p>Land and building elements are generally accounted for as a single unit, unless the land represents 25 percent or more of the total fair value of the leased property.</p>	<p>Land and building elements must be considered separately, unless the land element is not material. This means that nearly all leases involving land and buildings should be bifurcated into two components, with separate classification considerations and accounting for each component.</p> <p>In 2009 lease accounting was amended to provide guidance for classifying the land element of a lease. Previously, the land element of a lease was required to be classified as an operating lease unless title to the land was expected to pass to the lessee by the end of the lease term. That rule has been eliminated. Going forward, the lease of the land element should be classified based on a consideration of all of the risks and rewards indicators that apply to leases of other assets. Accordingly, a land lease would normally be classified as a finance lease if the lease term were long enough to cause the present value of the minimum lease payments to be at least substantially all of the fair value of the land. The new lease classification should be applied retrospectively at the effective date if the entity has the information to do so. If not, the new lease classification shall be applied as of the effective date.</p>

Impact	US GAAP	IFRS
Leases involving land and buildings (continued)		In determining whether the land element is an operating or a finance lease, an important consideration is that land normally has an indefinite economic life. A lessee is required to reassess the classification of land elements of unexpired leases at the date it adopts the amendment noted above on the basis of information existing at the inception of those leases.
Classification—other The exercise of renewal/extension options within leases may result in a new lease classification under US GAAP, but not under IFRS. Leveraged lease accounting is not available under IFRS, potentially resulting in delayed income recognition and gross balance sheet presentation.	The renewal or extension of a lease beyond the original lease term, including those based on existing provisions of the lease arrangement, normally triggers a fresh lease classification. The lessor can classify leases that would otherwise be classified as direct-financing leases as leveraged leases if certain additional criteria are met. Financial lessors sometimes prefer leveraged lease accounting because it often results in faster income recognition. It also permits the lessor to net the related nonrecourse debt against the leveraged lease investment in the balance sheet.	If the period covered by the renewal option was not considered to be part of the initial lease term, but the option is ultimately exercised based on the contractually stated terms of the lease, the original lease classification under the guidance continues into the extended term of the lease; it is not revisited. The guidance does not permit leveraged lease accounting. Leases that would qualify as leveraged leases under US GAAP would typically be classified as finance leases under IFRS. Any nonrecourse debt would be reflected gross on the balance sheet.

Impact	US GAAP	IFRS
<p>Classification—other (continued) Immediate income recognition by lessors on leases of real estate is more likely under IFRS.</p>	<p>Under the guidance, income recognition for an outright sale of real estate is appropriate only if certain requirements are met. By extension, such requirements also apply to a lease of real estate. Accordingly, a lessor is not permitted to classify a lease of real estate as a sales-type lease unless ownership of the underlying property automatically transfers to the lessee at the end of the lease term, in which case the lessor must apply the guidance appropriate for an outright sale.</p>	<p>The guidance does not have a similar provision. Accordingly, a lessor of real estate (e.g., a dealer) will recognize income immediately if a lease is classified as a finance lease (i.e., if it transfers substantially all the risks and rewards of ownership to the lessee).</p>
Other		
<p>Distributions of nonmonetary assets to owners Spin-off transactions under IFRS can result in gain recognition as nonmonetary assets are distributed at fair value. Nonmonetary assets are distributed at their recorded amount under US GAAP and no gains are recognized.</p>	<p>Accounting for the distribution of nonmonetary assets to owners of an enterprise should be based on the recorded amount (after reduction, if appropriate, for an indicated impairment of value) of the nonmonetary assets distributed. Upon distribution those amounts are reflected as a reduction of owner's equity.</p>	<p>Accounting for the distribution of nonmonetary assets to owners of an entity should be based on the fair value of the nonmonetary assets to be distributed. A dividend payable is measured at the fair value of the nonmonetary assets to be distributed. Upon settlement of a dividend payable, an entity will recognize the difference, if any, between the carrying amount of the assets to be distributed and the carrying amount of the dividend payable in profit or loss.</p>

Impact	US GAAP	IFRS
<p>Inventory costing</p> <p>Companies that utilize the LIFO-costing methodology under US GAAP may experience significantly different operating results as well as cash flows under IFRS. Furthermore, regardless of the inventory costing model utilized, under IFRS companies may experience greater earnings volatility in relation to recoveries in values previously written down.</p>	<p>A variety of inventory costing methodologies such as LIFO, FIFO and/or weighted-average cost are permitted. For companies using LIFO for US income tax purposes, the book/tax conformity rules also require the use of LIFO for book accounting/reporting purposes. Reversals of write-downs are prohibited.</p>	<p>A number of costing methodologies such as FIFO or weighted-average costing are permitted. The use of LIFO, however, is precluded. Reversals of inventory write-downs (limited to the amount of the original write-down) are required for subsequent recoveries.</p>
<p>Biological assets—fair value versus historical cost</p> <p>Companies whose operations include management of the transformation of living animals or plants into items for sale, agricultural produce or additional biological assets, have the potential for fundamental changes to their basis of accounting (because IFRS requires fair-value-based measurement).</p>	<p>Historical cost is generally used for biological assets. These assets are tested for impairment in the same manner as other long-lived assets.</p>	<p>The accounting treatment for biological assets requires measurement at fair value less costs to sell at initial recognition of biological assets and at each subsequent reporting date. It is possible to avoid the use of fair value on initial recognition only when the measurement of fair value is “clearly unreliable.” All changes in fair value are recognized in the statement of operations in the period in which they arise.</p>

Impact	US GAAP	IFRS
Investment property Alternative methods or options of accounting for investment property under IFRS could result in significantly different asset carrying values (fair value) and earnings.	<p>There is no specific definition of investment property.</p> <p>The historical-cost model is used for most real estate companies and operating companies holding investment-type property.</p> <p>Investor entities—such as many investment companies, insurance companies' separate accounts, bank-sponsored real estate trusts and employee benefit plans that invest in real estate—carry their investments at fair value.</p> <p>The fair value alternative for leased property does not exist.</p>	<p>Property (land and/or buildings) held in order to earn rentals and/or for capital appreciation is separately defined. The definition does not include owner occupied property, property held for sale in the ordinary course of business or property being constructed or developed. Properties under construction or development for future use as investment properties are within the scope of investment properties.</p> <p>Investment property may be accounted for on a historical-cost basis or on a fair value basis. When fair value is applied, the gain or loss arising from a change in the fair value is recognized in the statement of operations. The carrying amount is not depreciated.</p> <p>The election to account for investment property at fair value can also be applied to leased property.</p>
Technical references		
IFRS	IAS 2, IAS 16, IAS 17, IAS 23, IAS 36, IAS 37, IAS 40, IAS 41, IFRS 5, IFRIC 4, SIC 15, IFRIC 17	
US GAAP	ASC 205, ASC 250, ASC 330, ASC 360-10, ACS 360-20, ASC 410-20, ASC 410-20-25, ASC 835-20, ASC 840, ASC 840-40, ASC 976	

Note

The foregoing discussion captures a number of the more significant GAAP differences. It is important to note that the discussion is not inclusive of all GAAP differences in this area.

Recent/proposed guidance

Leases—joint project of the IASB and FASB

The IASB and the FASB are carrying out a project with the objective of comprehensively reconsidering the ASC 840 guidance on accounting for leases, and IAS 17, *Leases*, along with subsequent amendments and interpretations, to ensure that financial statements provide useful, transparent and complete information about leasing transactions for investors and other users of financial statements. In March 2009, the Boards (i.e., the FASB and IASB) published, for public comment, a Discussion Paper, *Leases: Preliminary Views*. Comments were due in July 2009. Under the new proposal:

- Lease accounting would significantly change, including the elimination of operating lease accounting by lessees.
- Lessees would treat all leases, including those in effect when the new standard is issued, in a manner similar to how capital leases are accounted for today.
- The proposal would require lessees to reassess the lease term, contingent rentals, residual value guarantees and the corresponding lease obligation at each reporting date using current facts and circumstances.

The proposed accounting model for leases is expected to have the greatest impact on lessees of significant amounts of “large-ticket” items, such as real estate, manufacturing equipment, power plants, aircraft, railcars, and ships. However, the proposed accounting model would also affect virtually every company across all industries to varying degrees.

The Boards will consider responses to the Discussion Paper as they further develop the proposed model working toward issuing an exposure draft. The Boards plan to issue an exposure draft in 2010, with a final standard expected in 2011.

Assets—financial assets

Under US GAAP, various specialized pronouncements provide guidance for the classification of financial assets. IFRS has only one standard for the classification of financial assets and requires that financial assets be classified in one of four categories: assets held for trading or carried at fair value, with changes in fair value reported in earnings; held-to-maturity investments; available-for-sale financial assets; and loans and receivables. The specialized US guidance and the singular IFRS guidance in relation to classification are particularly important because they can drive differences in both classification and measurement (since classification drives measurement under both IFRS and US GAAP).

A detailed discussion of industry-specific differences is beyond the scope of this publication. However, for illustrative purposes only, we note that the accounting under US GAAP for unlisted equity securities can differ substantially depending on industry-specific requirements. US GAAP accounting by general corporate entities that do not choose the fair value option, for example, differs significantly from accounting by broker/dealers, investment companies and insurance companies. In contrast, the guidance in relation to unlisted equity securities under IFRS is the same regardless of the industry in which the entity in question operates.

Under US GAAP, classification is driven by the legal form of the financial asset. For example, debt instruments that are legal form securities are typically carried at fair value under the available-for-sale category (unless they are held-to-maturity)—even if there is no active market to trade the securities. At the same time, a debt instrument (for example, a corporate loan) is accounted for at amortized cost even though both instruments (i.e., the security and the loan) have similar economic characteristics. Under IFRS, the legal form does not drive classification of debt instruments—rather, the nature of the instrument (including whether there is an active market) is considered. Additional differences involve financial assets that are carried at amortized cost. For such assets, both IFRS and US GAAP use the effective interest method to calculate amortized cost and allocate interest income over the relevant period. The effective interest method is based on the effective interest rate calculated at initial recognition of the financial instrument. Under IFRS, the effective interest rate is calculated based on estimated future cash payments or receipts through the expected life of the financial instrument. Under US GAAP, although certain exceptions apply, the effective interest rate is generally calculated based on the contractual cash flows through the contractual life of the financial assets, adjusted for unanticipated changes in the instrument's estimated cash flows. Under IFRS, changes in the estimated cash flows due to a closely related embedded derivative that is not bifurcated results in a cumulative catch-up reflected in the current-period income statement. US GAAP does not have the equivalent of a cumulative catch-up-based approach for these scenarios.

For available-for-sale debt instruments, the impairment models for financial assets may result in different impairment triggers and different impairment measurement criteria. In considering whether a decline in fair value is other than temporary, US GAAP looks to 1) management's intent and ability to hold the security and 2) expectations of recovery of the cost basis in the security. The impairment trigger drives the measurement of the impairment loss. Under IFRS, the impairment triggers for available-for-sale debt instruments and loans and receivables are the same—however, the available-for-sale impairment loss is based on fair value while impairment of loans and receivables is calculated by discounting cash flows adjusted for incurred loss by the original effective interest rate. Additional differences around reversals of impairment losses and impairment of equities must also be considered.

There are fundamental differences in the way US GAAP and IFRS assess the potential derecognition of financial assets. The differences can have significant impact on a variety of transactions such as asset securitizations. IFRS focuses on whether a qualifying

transfer has taken place, whether risks and rewards have been transferred and, in some cases, whether control over the asset(s) in question has been transferred. US GAAP focuses on whether an entity has surrendered control over an asset, including the surrendering of legal and effective control. The fundamental differences are as follows:

- Under US GAAP, derecognition can be achieved even if the transferor has significant ongoing involvement with the assets, such as the retention of significant exposure to credit risk.
- Under IFRS, full derecognition can be achieved only if substantially all of the risks and rewards are transferred or the entity has neither retained nor transferred substantially all of the risks and rewards and the transferee has the practical ability to sell the transferred asset.
- Under IFRS, if the entity has neither retained nor transferred substantially all of the risks and rewards and if the transferee does not have the practical ability to sell the transferred asset, the transferor continues to recognize the transferred asset with an associated liability in a unique model known as the continuing involvement model, which has no equivalent under US GAAP.

The IFRS model does not permit many factoring transactions (e.g., sale of receivables with recourse) to qualify for derecognition. Most factorings include some ongoing involvement by the transferor that causes the transferor to retain some of the risks and rewards related to the transferred assets—a situation that may preclude full derecognition under IFRS, but not under US GAAP.

Further details on the foregoing and other selected differences are described in the following table.

Impact	US GAAP	IFRS
Classification and measurement		
Available-for-sale financial assets: fair value versus cost of unlisted equity instruments More investments in unlisted equity securities are recorded at fair value under IFRS.	<p>Unlisted equity investments generally are scoped out of ASC 320 and would be carried at cost, unless either impaired or the fair value option is elected.</p> <p>Certain exceptions requiring that investments in unlisted equity securities be carried at fair value do exist for specific industries (e.g., broker/dealers, investment companies, insurance companies, defined benefit plans).</p>	<p>There are no industry-specific differences in the treatment of investments in equity instruments that do not have quoted market prices in an active market. Rather, all available-for-sale assets, including investments in unlisted equity instruments, are measured at fair value (with rare exceptions only for instances where fair value cannot be reliably measured).</p> <p>Fair value is not reliably measurable when the range of reasonable fair value estimates is significant and the probability of the various estimates within the range can not be reasonably assessed.</p>

Impact	US GAAP	IFRS
<p>Available-for-sale debt financial assets: foreign exchange gains/losses on debt instruments</p> <p>The treatment of foreign exchange gains and losses on available-for-sale debt securities will create more income statement volatility under IFRS.</p>	<p>The <i>total</i> change in fair value of available-for-sale debt securities—net of associated tax effects—is recorded within other comprehensive income.</p> <p>Any component of the overall change in fair market value that may be associated with foreign exchange gains and losses on an available-for-sale debt security is treated in a manner consistent with the remaining overall change in the instrument's fair value.</p>	<p>For available-for-sale debt instruments, the total change in fair value is bifurcated, with the portion associated with foreign exchange gains/losses separately recognized in the income statement. The remaining portion of the total change in fair value is recognized in a separate component of equity, net of tax effect.</p>
<p>Effective interest rates: expected versus contractual cash flows</p> <p>Differences between the expected and contractual lives of financial assets carried at amortized cost have different implications under the two frameworks.</p> <p>The difference in where the two accounting frameworks place their emphasis (contractual term for US GAAP and expected outcome for IFRS) can affect asset carrying values and the timing of income recognition.</p>	<p>For financial assets that are carried at amortized cost, the calculation of the effective interest rate is generally based on <i>contractual</i> cash flows over the asset's <i>contractual</i> life.</p> <p>The expected life, under US GAAP, is typically used only for:</p> <ol style="list-style-type: none"> 1. loans if the entity holds a large number of similar loans and the prepayments can be reasonably estimated; 2. certain structured notes; 3. certain beneficial interests in securitized financial assets; and 4. certain loans or debt securities acquired in a transfer. 	<p>For financial assets that are carried at amortized cost, the calculation of the effective interest rate is generally based on the <i>estimated</i> cash flows over the <i>expected</i> life of the asset.</p> <p>Contractual cash flows over the full contractual term of the financial asset are used only in those rare cases when it is not possible to reliably estimate the expected cash flows over the expected life of a financial asset.</p>

Impact	US GAAP	IFRS
<p>Effective interest rates: changes in expectations</p> <p>Differences in how changes in expectations (associated with financial assets carried at amortized cost) are treated can affect asset valuations and the timing of income statement recognition.</p>	<p>Different models apply to the ways revised estimates are treated depending on the type of financial asset involved (e.g., structured notes, beneficial interests, loans or debt acquired in a transfer).</p> <p>Depending on the nature of the asset, changes may be reflected prospectively or retrospectively. Typically, the US GAAP model ignores the changes in current interest rates. None of the US GAAP models is the equivalent of the IFRS cumulative-catch-up-based approach.</p>	<p>If an entity revises its estimates of payments or receipts, the entity adjusts the carrying amount of the financial asset (or group of financial assets) to reflect both actual and revised estimated cash flows.</p> <p>Frequent revisions of the estimated life or of the estimated future cash flows may exist, for example, in connection with debt instruments that contain a put or call option that doesn't need to be bifurcated or whose coupon payments vary, because of an embedded feature that does not meet the definition of a derivative because its underlying is a nonfinancial variable specific to a party to the contract (e.g., cash flows that are linked to earnings before interest, taxes, depreciation and amortization; sales volume; or the earnings of one party to the contract).</p> <p>The entity recalculates the carrying amount by computing the present value of estimated future cash flows at the financial asset's original effective interest rate. The adjustment is recognized as income or expense in the income statement (i.e., by the cumulative-catch-up approach).</p> <p>Generally, floating rate instruments (e.g., LIBOR plus spread) issued at par are not subject to the cumulative catch-up approach; rather the effective interest rate is revised as market rates change.</p>

Impact	US GAAP	IFRS
<p>Fair value option for equity-method investments</p> <p>While both accounting standards include a fair value option for equity-method investments, the IFRS-based option has limits as to which entities can exercise it, whereas the US GAAP option is broad based.</p>	<p>The fair value option exists for US GAAP entities under ASC 825, <i>Financial Instruments</i>, wherein the option is unrestricted. Therefore, any investor's equity method investments are eligible for the fair value option.</p>	<p>IFRS permits venture capital organizations, mutual funds and unit trusts (as well as similar entities, including investment-linked insurance funds) that have investments in associates (entities over which they have significant influence) to carry those investments at fair value, with changes in fair value reported in earnings (provided certain criteria are met) in lieu of applying equity-method accounting.</p>
<p>Fair value measurement: bid-ask spreads</p> <p>Differences in the ways bid-ask spreads are treated may affect financial asset valuations. At the same time, the recognition of Day One gains will be less frequent under IFRS.</p>	<p>If an input used for measuring fair value is based on bid and ask prices, the price within the bid-ask spread that is most representative of fair value in the circumstances is used. At the same time, US GAAP does not preclude the use of midmarket pricing or other pricing conventions as practical expedients for fair value measurements within a bid-ask spread. As a result, financial assets may, in certain situations, be valued at a bid or ask price, at the last price, at the mean between bid and ask prices or at a valuation within the range of bid and ask prices.</p>	<p>The appropriate quoted market price for an asset held or a liability to be issued is the current bid price and, for an asset to be acquired or a liability held, is the ask price. However, when the entity has assets and liabilities with offsetting market positions, the entity may use the midprice for the offsetting positions and apply the bid or ask price to the net open position.</p>

Impact	US GAAP	IFRS
<p>Loans and receivables</p> <p>Classification is not driven by legal form under IFRS, whereas legal form drives the classification of “debt securities” under US GAAP. The potential classification differences drive subsequent measurement differences under IFRS and US GAAP for the same debt instrument.</p> <p>Loans and receivables may be carried at different amounts under the two frameworks.</p>	<p>The classification and accounting treatment of non-derivative financial assets such as loans and receivables generally depend on whether the asset in question meets the definition of a debt security under ASC 320. If the asset meets that definition, it is generally classified as either trading, available-for-sale or held-to-maturity. If classified as trading or available-for-sale, the debt security is carried at fair value. To meet the definition of a debt security under ASC 320, the asset is required to be of a type commonly available on securities exchanges or in markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment.</p> <p>Loans and receivables that are not within the scope of ASC 320 fall within the scope of other guidance. As an example, mortgage loans are either:</p> <ul style="list-style-type: none"> • Classified as loans held for investment, in which case they are measured at amortized cost; • Classified as loans held for sale, in which case they are measured at the lower of cost or fair value (market); or • Carried at fair value if the fair value option is elected. 	<p>IFRS defines loans and receivables as non-derivative financial assets with fixed or determinable payments not quoted in an active market and that are other than:</p> <ul style="list-style-type: none"> • Those that the entity intends to sell immediately or in the near term, which are classified as held for trading and those that the entity upon initial recognition designates as at fair value through profit or loss; • Those that the entity upon initial recognition designates as available-for-sale; and • Those for which the holder may not recover substantially all of its initial investment (other than because of credit deterioration) and that shall be classified as available-for-sale. <p>An interest acquired in a pool of assets that are not loans or receivables (i.e., an interest in a mutual fund or a similar fund) is not a loan or receivable.</p> <p>Instruments that meet the definition of loans and receivables (regardless of whether they are legal form securities) are carried at amortized cost in the loan and receivable category unless classified into either the fair value through profit-or-loss category or the available-for-sale category. In either of the latter two cases, they are carried at fair value.</p> <p>IFRS does not have a category of loans and receivables that is carried at the lower of cost or market.</p>

Impact	US GAAP	IFRS
<p>Reclassifications</p> <p>Transfers of financial assets into or out different categories are permitted in limited circumstances under both frameworks. In general, reclassifications have the potential to be more common under IFRS. The ability to reclassify is impacted by initial classification, which can also vary (as discussed above).</p>	<p>Changes in classification between trading, available-for-sale and held-to-maturity categories occur only when justified by the facts and circumstances within the concepts of ASC 320. Given the nature of a trading security, transfers into or from the trading category should be rare, though they do occur.</p>	<p>Financial assets may be reclassified between categories, albeit with conditions.</p> <p>More significantly, debt instruments may be reclassified from held for trading or available-for-sale into loan and receivable, if the debt instrument meets the definition of loans and receivables and the entity has the intent and ability to hold for the foreseeable future.</p> <p>Also, a financial asset can be transferred from trading to available-for-sale in rare circumstances.</p> <p>Reclassification is prohibited for instruments where the fair value option is elected.</p>
Impairments and subsequent loss treatment		
<p>Impairment principles: available-for-sale debt securities</p> <p>Regarding impairment triggers, IFRS focuses on events that affect the recovery of the cash flows from the asset regardless of the entity's intent. US GAAP looks to a two-step test based on intent or ability to hold and expected cash flows.</p> <p>Regarding measurement of impairment loss upon a trigger, IFRS uses fair value less amortized cost. Under US GAAP, the impairment loss depends on the triggering event.</p>	<p>An investment in debt securities is assessed for impairment if the fair value is less than cost. An analysis is performed to determine whether the shortfall in fair value is temporary or other than temporary.</p> <p>In a determination of whether impairment is other than temporary, the following factors are assessed for available-for-sale securities:</p> <p>Step 1— Can management assert (a) it does not have the intent to sell and (b) it is more likely than not that it will not have to sell before recovery of cost? If no, then impairment is triggered. If yes, then move to Step 2.</p>	<p>A financial asset is impaired and impairment losses are incurred only if there is objective evidence of impairment as the result of one or more events that occurred after initial recognition of the asset (a loss event) and if that loss event has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be estimated reliably. In assessing the objective evidence of impairment, an entity considers the following factors:</p> <ul style="list-style-type: none"> • Significant financial difficulty of the issuer • High probability of bankruptcy • Granting of a concession to the issuer

Impact	US GAAP	IFRS
Impairment principles: available-for-sale debt securities (continued)	<p>Step 2—Does management expect recovery of the entire cost basis of the security? If yes, then impairment is not triggered. If no, then impairment is triggered:</p> <p>Once it is determined that impairment is other than temporary, the impairment loss recognized in the income statement depends on the impairment trigger:</p> <ul style="list-style-type: none"> If impairment is triggered as a result of Step 1, the loss in equity due to changes in fair value is released into the income statement. If impairment is triggered in Step 2, impairment loss is measured by calculating the present value of cash flows expected to be collected from the impaired security. The determination of such expected credit loss is not explicitly defined; one method could be to discount the best estimate of cash flows by the original effective interest rate. The difference between the fair value and the post impairment amortized cost is recorded within other comprehensive income. 	<ul style="list-style-type: none"> Disappearance of an active market because of financial difficulties Breach of contract, such as default or delinquency in interest or principal Observable data indicating there is a measurable decrease in the estimated future cash flows since initial recognition <p>The disappearance of an active market because an entity's securities are no longer publicly traded or the downgrade of an entity's credit rating is not, by itself, evidence of impairment, although it may be evidence of impairment when considered with other information.</p> <p>At the same time, a decline in the fair value of a debt instrument below its amortized cost is not necessarily evidence of impairment. For example, a decline in the fair value of an investment in a corporate bond that results solely from an increase in market interest rates is not an impairment indicator and would not require an impairment evaluation under IFRS.</p> <p>An impairment analysis under IFRS focuses only on the triggering events that affect the cash flows from the asset itself and does not consider the holder's intent.</p> <p>Once impairment of a debt instrument is determined to be triggered, the loss in equity due to changes in fair value is released into the income statement.</p>

Impact	US GAAP	IFRS
<p>Impairment principles: held-to-maturity debt instruments</p> <p>Regarding impairment triggers, IFRS focuses on events that affect the recovery of the cash flows from the asset regardless of the entity's intent. US GAAP looks to a two-step test based on intent or ability to hold and expected cash flows.</p> <p>Regarding measurement of impairment loss upon a trigger, IFRS looks to incurred loss amount. Under US GAAP, the impairment loss depends on the triggering event.</p>	<p>The two-step impairment test mentioned above is also applicable to investments classified as held-to-maturity. It would be expected that held-to-maturity investments would not trigger Step 1 (as tainting would result). Rather, evaluation of Step 2 may trigger impairment.</p> <p>Once triggered, impairment is measured with reference to expected credit losses as described for available-for-sale debt securities. The difference between the fair value and the post impairment amortized cost is recorded within other comprehensive income and accreted from other comprehensive income to the amortized cost of the debt security over its remaining life prospectively.</p>	<p>Impairment is triggered for held-to-maturity investments based on objective evidence of impairment described above for available-for-sale debt instruments.</p> <p>Once impairment is triggered, the loss is measured by discounting the estimated future cash flows (adjusted for incurred loss) by the original effective interest rate. As a practical expedient, impairment may be measured based on the instrument's observable fair value.</p>

Impact	US GAAP	IFRS
<p>Impairment of available-for-sale equity instruments</p> <p>Impairment on available-for-sale equity instruments may be triggered at different points in time under IFRS compared to US GAAP.</p>	<p>US GAAP looks to whether the decline in fair value below cost is other-than-temporary. The factors to consider include:</p> <ul style="list-style-type: none"> • The length of the time and the extent to which the market value has been less than cost; • The financial condition and near-term prospects of the issuer, including any specific events that may influence the operations of the issuer, such as changes in technology that may impair the earnings potential of the investment or the discontinuance of a segment of the business that may affect the future earnings potential; and • The intent and ability of the holder to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in market value. <p>The evaluation of the other-than-temporary impairment trigger requires significant judgment in assessing the recoverability of decline in fair value below cost. Generally, the longer the decline and the greater the decline, the more difficult it is to overcome that the available-for-sale equity is other than temporarily impaired.</p>	<p>Similar to debt investments, impairment of available-for-sale equity investments is triggered by objective evidence of impairment. In addition to examples of events discussed above, objective evidence of impairment of AFS equity includes:</p> <ul style="list-style-type: none"> • Significant decline in fair value below cost; • Prolonged decline in fair value cost; or • Significant adverse changes in technological, market, economic or legal environment. <p>Each factor on its own could trigger impairment (i.e., the decline in fair value below cost does not need to be both significant and prolonged).</p> <p>For example, if a decline has persisted for more than 12 consecutive months, then the decline is likely to be considered “prolonged.”</p> <p>Whether a decline in fair value below cost is considered as significant must be assessed on an instrument-by-instrument basis and should be based on both qualitative and quantitative factors.</p>

Impact	US GAAP	IFRS
<p>Losses on available-for-sale equity securities subsequent to initial impairment recognition</p> <p>In periods after the initial recognition of an impairment loss on available-for-sale equity securities, further income statement charges are more likely under IFRS.</p>	<p>Impairment charges establish a new cost basis. As such, further reductions in value below the new cost basis may be considered temporary (when compared with the new cost basis).</p>	<p>Impairment charges do not establish a new cost basis. As such, further reductions in value below the original impairment amount are recorded within the current-period income statement.</p>
<p>Impairments: measurement and reversal of losses</p> <p>Under IFRS, impairment losses on debt instruments may be reversed through the income statement. Under US GAAP, reversals are permitted for debt instruments classified as loans; however, one-time reversal of impairment losses on debt securities is prohibited. Expected recoveries are reflected over time by adjusting the interest rate to accrue interest income.</p>	<p>Impairments of loans held for investment measured under ASC 310-10-35 and ASC 450 are permitted to be reversed; however, the carrying amount of the loan can at no time exceed the recorded investment in the loan.</p> <p>One-time reversals of impairment losses for debt securities classified as available-for-sale or held-to-maturity securities, however, are prohibited. Rather, any expected recoveries in future cash flows are reflected as a prospective yield adjustment.</p> <p>Reversals of impairments on equity investments are prohibited.</p>	<p>For financial assets carried at amortized cost, if in a subsequent period the amount of impairment loss decreases and the decrease can be objectively associated with an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed. The reversal, however, does not exceed what the amortized cost would have been had the impairment not been recognized.</p> <p>For available-for-sale debt instruments, if in a subsequent period the fair value of the debt instrument increases and the increase can be objectively related to an event occurring after the loss was recognized, the loss may be reversed through the income statement.</p> <p>Reversals of impairments on equity investments are prohibited.</p>

Impact	US GAAP	IFRS
Asset derecognition		
<p>Derecognition</p> <p>The determination of whether or not financial assets should be derecognized (e.g., in securitizations or factorings) is based on very different models under the two frameworks.</p> <p>Recent guidance will tend to reduce the frequency of achieving derecognition under US GAAP. Full derecognition under US GAAP will, however, still be more common than under IFRS. Having said that, the IFRS model includes continuing involvement presentation that has no equivalent under US GAAP.</p>	<p>The guidance focuses on an evaluation of the transfer of control. The evaluation is governed by three key considerations:</p> <ul style="list-style-type: none"> • Legal isolation of the transferred asset from the transferor • The ability of the transferee (or if the transferee is a securitization vehicle, the beneficial interest holder) to pledge or exchange the asset (or the beneficial interest holder) • No right or obligation of the transferor to repurchase <p>As such, derecognition can be achieved even if the transferor has significant ongoing involvement with the assets, such as the retention of significant exposure to credit risk.</p> <p>ASC 860 is applied before consolidation guidance is considered.</p> <p>Therefore, even if the transfer criteria are met, the transferor may not achieve derecognition as the assets may be, in effect, transferred to the consolidated entity.</p>	<p>The guidance focuses on evaluation of whether a qualifying transfer has taken place, whether risks and rewards have been transferred and, in some cases, whether control over the asset(s) in question has been transferred.</p> <p>The transferor first applies the consolidation guidance and consolidates any and all subsidiaries or special purpose entities (SPEs) it controls.</p> <p>Under IAS 39, full derecognition is appropriate once both of the following conditions have been met:</p> <ul style="list-style-type: none"> • The financial asset has been transferred outside the consolidated group. • The entity has transferred substantially all of the risks and rewards of ownership of the financial asset.

Impact	US GAAP	IFRS
Derecognition (continued)	<p>There is no concept of continuing involvement/partial derecognition under US GAAP.</p> <p>When accounting for a transfer of an individual financial asset or a group of financial assets that qualifies as a sale, the assets transferred in the sale must be derecognized from the transferor's balance sheet. The total carrying amount of the asset is derecognized and any assets and liabilities retained are recognized at fair value. The transferor should separately recognize any servicing assets or servicing liabilities retained in the transfer at their fair values. A gain or loss on the transfer is calculated as the difference between the net proceeds received and the carrying value of the assets sold.</p>	<p>The first condition is achieved in one of two ways:</p> <ul style="list-style-type: none"> • When an entity transfers the contractual rights to receive the cash flows of the financial asset; or • When an entity retains the contractual rights to the cash flows, but assumes a contractual obligation to pass the cash flows on to one or more recipients (referred to as a pass-through arrangement). <p>Many securitizations do not meet the strict pass-through criteria to recognize a transfer of the asset outside of the consolidated group and as a result fail the first condition for derecognition.</p> <p>As for the risks and rewards criterion, many securitization transactions include some ongoing involvement by the transferor that causes the transferor to retain substantial risks and rewards, thereby failing the second condition for derecognition, even if the pass-through test is met.</p>

Impact	US GAAP	IFRS
Derecognition (continued)		<p>When an asset transfer has been accomplished, but the entity has neither retained nor transferred substantially all risks and rewards, an assessment as to control becomes necessary. The transferor assesses whether the transferee has the practical ability to sell the asset transferred to a third party. The emphasis is on what the transferee can do in practice and whether it is able, unilaterally, to sell the transferred asset. If the transferee does not have the ability to sell the transferred asset, control is deemed to be retained by the transferor and the transferred asset may require a form of partial derecognition called continuing involvement. Under continuing involvement, the transferred asset continues to be recognized with an associated liability.</p> <p>When the entity has continuing involvement in the transferred asset, the entity must continue to recognize the transferred asset to the extent of its exposure to changes in the value of the transferred asset. Continuing involvement is measured as either the maximum amount of consideration received that the entity could be required to repay (in the case of guarantees) or the amount of the transferred asset that the entity may repurchase (in the case of a repurchase option).</p>

Technical references

IFRS IAS 39, SIC 12

US GAAP ASC 310, ASC 310-10-30, ASC 310-10-35, ASC 320, ASC 325, ASC 815, ASC 815-15-25-4 through 25-5, ASC 820, ASC 825, ASC 860

Note

The foregoing discussion captures a number of the more significant GAAP differences. It is important to note that the discussion is not inclusive of all GAAP differences in this area.

Recent/proposed guidance***ASC 820-10-65-4: Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly***

This provides additional guidance for estimating fair value in accordance with fair value instruments when the volume and level of activity for the asset or liability have significantly decreased. This FSP also includes guidance on identifying circumstances that indicate a transaction is not orderly.

This guidance emphasizes that even if there has been a significant decrease in the volume and level of activity for the asset or liability and regardless of the valuation technique(s) used, the objective of a fair value measurement remains the same. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions.

This guidance is effective for interim and annual reporting periods ending after June 15, 2009, and shall be applied prospectively.

The guidance provided is consistent with that provided by the IASB's Expert Advisory Panel report and fair value measurement exposure draft.

ASC 320-10-65-1: Recognition and Presentation of Other-Than-Temporary Impairments

This guidance amends the other-than-temporary impairment guidance in US GAAP for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments on debt and equity securities in the financial statements. This FSP does not amend existing recognition and measurement guidance related to other-than-temporary impairments of equity securities.

The objective of an other-than-temporary impairment analysis under existing US GAAP is to determine whether the holder of an investment in a debt or equity security for which changes in fair value are not regularly recognized in earnings (such as securities classified as held-to-maturity or available-for-sale) should recognize a loss in earnings when the investment is impaired. An investment is impaired if the fair value of the investment is less than its amortized cost basis (as discussed in the table above in the impairment section).

This is effective for interim and annual reporting periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009.

For details, refer to the discussion under the impairment principles: available-for-sale and held-to-maturity debt instruments sections above.

ASC 320-10-99-1: Other Than Temporary Impairment of Certain Investments in Debt and Equity Securities

This guidance amends Topic 5.M. in the Staff Accounting Bulletin Series titled *Other Than Temporary Impairment of Certain Investments in Debt and Equity Securities* (Topic 5.M.). On April 9, 2009, the FASB issued guidance on the recognition and presentation of other-than-temporary impairments to provide guidance for assessing whether an impairment of a debt security is other than temporary. The guidance refers to this SAB for a discussion of considerations applicable to a determination as to whether a decline in market value below cost of an equity security, at a particular point in time, is other than temporary. Topic 5.M. (as amended) maintains the staff's previous views related to equity securities and amends Topic 5.M. to exclude debt securities from its scope.

Accounting for Transfers of Financial Assets

This amends the guidance on transfers of financial assets in order to address practice issues highlighted most recently by events related to the economic downturn. The amendments include: (1) eliminating the qualifying special-purpose entity concept (QSPE), (2) a new unit of account definition that must be met for transfers of portions of financial assets to be eligible for sale accounting, (3) clarifications and changes to the derecognition criteria for a transfer to be accounted for as a sale, (4) a change to the amount of recognized gain or loss on a transfer of financial assets accounted for as a sale when beneficial interests are received by the transferor, and (5) extensive new disclosures.

Calendar year-end companies will have to apply this guidance to new transfers of financial assets occurring from January 1, 2010. Companies will need to assess how their financial statements and future transfers of financial assets will be affected.

This guidance is intended to address certain perceived flaws in US GAAP and is not intended to converge US GAAP with IFRS in this area although the elimination of the QSPE concept could be viewed as a step closer to convergence because IFRS does not have this concept). However, the FASB intends to work with the IASB in considering comment letters on its exposure draft and developing a final converged derecognition standard.

Amendments to IAS 39 and IFRS 7: Reclassification of Financial Assets

This amendment to the standards, issued in October 2008, permits an entity to reclassify non-derivative financial assets (other than those designated at fair value through profit or loss by the entity upon initial recognition) out of the held for trading category in particular circumstances. The amendment also permits an entity to transfer from the available-for-sale category to the loans and receivables category a financial asset that would have met the definition of loans and receivables (if the financial asset had not been designated as available-for-sale), if the entity has the intention and ability to hold that financial asset for the foreseeable future.

For details, refer to the discussion under "Reclassifications" above.

Exposure Draft, *Derecognition*: Proposed Amendments to IAS 39 and IFRS 7

In March 2009 the IASB issued Exposure Draft 2009/3, *Derecognition*, which would amend existing provisions of IAS 39. The main purpose of the exposure draft was to address the perceived complexities within IAS 39 and the resulting difficulty of application in practice.

The draft includes two approaches to the derecognition of financial assets: the “proposed model” based on control is favored by the majority of the Board; the “alternative view” is supported by the remaining five members. A failed sale results in the asset remaining on the balance sheet under both approaches, with the proceeds received recognized as a financial liability.

The existing model in IAS 39 is primarily “risks and rewards,” with a secondary “control” test where risks and rewards have neither been substantially transferred nor retained. “Control” takes center-stage in the “proposed model,” with a risks and rewards overlay in the form of a test for continuing involvement in the transferred asset.

Derecognition under the alternative approach is also based on control. If the entity has given up control over any of the cash flows of the asset, it no longer controls that asset and hence the asset is derecognized in its entirety. The concept of partial derecognition does not exist in this model. A new asset/liability is recognized for any continuing involvement in the asset retained.

Comments were due July 31, 2009.

If either of the models proposed in the amendment was adopted, the differences to US GAAP would remain.

Exposure Draft, *Fair Value Measurements*

In May 2009 the IASB issued Exposure Draft 2009/5, which would create a new standard on fair value measurement and would amend the provisions of several existing standards. The proposed IFRS defines fair value, establishes a framework for measuring fair value and requires disclosures about fair value measurements.

The Board’s objectives for publishing the proposed IFRS are:

- to establish a single source of guidance for all fair value measurements required or permitted by IFRSs to reduce complexity and improve consistency in their application;
- to clarify the definition of fair value and related guidance in order to communicate the measurement objective more clearly; and
- to enhance disclosures about fair value to enable users of financial statements to assess the extent to which fair value is used and to inform them about the inputs used to derive those fair values.

The proposed IFRS does not require additional fair value measurements.

The draft IFRS defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (an exit price). In the absence of an actual transaction at the measurement date, a fair value measurement assumes a hypothetical transaction in the most advantageous market for the asset or liability. A fair value measurement requires an entity to determine:

- the particular asset or liability that is the subject of the measurement (consistently with its unit of account)
- for an asset, the valuation premise that is appropriate for the measurement (consistently with its highest and best use)

- the most advantageous market for the asset or liability
- the valuation technique(s) appropriate for the measurement, considering the availability of data with which to develop inputs that represent the assumptions that market participants would use in pricing the asset or liability and the level of the fair value hierarchy within which the inputs are categorized

As drafted the exposure draft would eliminate some but not all of the current US GAAP differences in this area.

Measuring and disclosing the fair value of financial instruments in markets that are no longer active—IASB Expert Advisory Panel

In May 2008, and in response to the recommendations of the Financial Stability Forum in its report *Enhancing Market and Institutional Resilience* (April 2008), the IASB formed an expert advisory panel. The panel identified practices that experts use for measuring and disclosing financial instruments when markets are no longer active. A summary of the panel's discussions were set out in *Measuring and disclosing the fair value of financial instruments in markets that are no longer active*. The document addresses:

- The fair value measurement objective
- Using prices from inactive markets
- Forced transactions
- Management's estimates in a fair value measurement
- Using broker quotes and information from pricing services

Financial Instruments: Replacement of IAS 39

In March 2008 the IASB released a discussion paper that discusses the main causes of complexity in reporting financial instruments. It also discusses possible intermediate and long-term approaches to improving financial reporting and reducing complexity. The IASB has noted that many preparers of financial statements, their auditors and users of financial statements find the requirements for reporting financial instruments complex. The IASB and the FASB have been urged by many to develop new standards of financial reporting for financial instruments that are principles-based and less complex than today's requirements.

As a result of the financial crisis, work on this project was accelerated to change the accounting for financial instruments. The replacement of IAS 39 project is being broken down into three stages, (1) classification and measurement of financial assets and liabilities, (2) impairment and (3) hedge accounting. The IASB is expected to release exposures drafts over the remainder of 2009 with classification and measurement already released in July 2009, impairment in October 2009 and hedge accounting in December 2009 with final standards in time for year end financial statements for 2009 (classification and measurement) and during 2010 (impairment and hedge accounting). The classification and measurement project is expected to eliminate the requirement to evaluate embedded derivatives in financial instruments.

This project has the potential to create significant differences when compared to current US GAAP. However, both the IASB and FASB are coordinating efforts in their projects to reduce complexity in reporting financial instruments, although the ultimate standards may not be fully converged.

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Liabilities

Liabilities—taxes

Although the two frameworks share many fundamental principles, they are at times conceptualized and applied in different manners. Differences in the calculations of liabilities and deferred taxes will likely result in a number of required adjustments in a company's tax accounts. The IASB released an exposure draft that would revise several areas of income tax accounting (see the Recent/proposed Guidance section at the end of this chapter), but would not eliminate all of the differences between US GAAP and IFRS. The following represent some of the more significant existing differences between the two frameworks.

In 2006, the FASB issued guidance surrounding the accounting for uncertainty in income taxes. To date, no similar detailed income tax specific guidance has been issued by the IASB, nor is this a difference that is expected to be resolved by the IASB's revision to its income tax guidance. Differences in both the unit-of-account methodology and the measurement methodology for uncertain tax positions may result in varying outcomes under the two frameworks.

Under US GAAP, any income tax effects resulting from intragroup profits are deferred at the seller's tax rate and recognized upon sale to a third party. IFRS requires the recording of deferred taxes based on the buyer's tax rate at the time of the initial transaction.

The tax rate applied when calculating deferred and current taxes may differ depending upon the framework used. At the same time, under IFRS, a single asset or liability may have more than one tax basis whereas there would generally only be one tax basis per asset or liability under US GAAP.

Differences in subsequent changes to deferred taxes recorded for certain equity-related items could result in less volatility in the income statement under IFRS. At the same time, the opposite impact (i.e., additional volatility) could result when share-based equity awards are considered. Under both US GAAP and IFRS, entities generally initially record their deferred taxes through the income statement unless the related item was recorded directly into equity or as an adjustment to goodwill. Under IFRS, all future increases or decreases in equity-related deferred tax asset or liability accounts are traced back to equity. Under US GAAP, however, subsequent changes arising as a result of tax rate and law changes on deferred taxes are recorded through the income statement even if the related deferred taxes initially arose in equity.

Presentation differences related to deferred taxes could affect the calculation of certain ratios from the face of the balance sheet—including a company's current ratio—because IFRS requires all deferred taxes to be classified as noncurrent.

Impact	US GAAP	IFRS
Uncertain tax positions Differences with respect to both the unit-of-account methodology and the measurement methodology may result in varying outcomes under the two frameworks.	<p>Uncertain tax positions are recognized and measured using a two-step process, first determining whether a benefit may be recognized and subsequently measuring the amount of the benefit. Tax benefits from uncertain tax positions can be recognized only if it is more likely than not that the tax position is sustainable based on its technical merits.</p> <p>Uncertain tax positions are evaluated at the individual tax position level.</p> <p>The tax position is measured by using a cumulative probability model: the largest amount of tax benefit that is greater than 50 percent likely of being realized upon ultimate settlement.</p>	<p>Accounting for uncertain tax positions is not specifically addressed within IFRS. The tax consequences of events should follow the manner in which an entity expects the tax position to be resolved (through either payment or receipt of cash) with the taxation authorities at the balance sheet date.</p> <p>Practice has developed such that uncertain tax positions may be evaluated at the level of the individual uncertainty or group of related uncertainties. Alternatively, they may be considered at the level of total tax liability to each taxing authority.</p> <p>Acceptable methods by which to measure tax positions include (1) the expected-value/probability-weighted-average approach and (2) the single-best-outcome/most-likely-outcome method. Use of the cumulative probability model required by US GAAP is not supported by IFRS.</p>
Unrealized intragroup profits The frameworks require different approaches when deferred taxes on unrealized intragroup activity are considered.	<p>Any tax impacts to the seller as a result of the intercompany sale are deferred and are realized upon the ultimate third-party sale.</p> <p>The buyer is prohibited from recognizing deferred taxes resulting from the intra-group sale.</p>	<p>Any tax impacts to the seller as a result of the intercompany transaction are recognized as incurred.</p> <p>Deferred taxes resulting from the intra-group sale are recognized at the buyer's tax rate.</p>

Impact	US GAAP	IFRS
Intraperiod allocations Differences in subsequent changes to deferred taxes could result in less volatility in the statement of operations under IFRS.	<p>Subsequent changes in deferred tax balances due to enacted tax rate and tax law changes are taken through the income statement regardless of whether the deferred tax was initially created through the income statement, through equity or in purchase accounting.</p> <p>Changes in the amount of valuation allowance due to changes in assessment about realization in future periods are generally taken through the income statement, with limited exceptions for certain equity-related items.</p>	<p>Subsequent changes in deferred tax balances are recognized in the income statement—except to the extent that the tax arises from a transaction or event that is recognized, in the same or a different period, directly in equity.</p>
Deferred taxes on investments in subsidiaries, joint ventures and equity investees Differences in the recognition criteria surrounding undistributed profits and other outside basis differences could result in changes in recognized deferred taxes under IFRS.	<p>With respect to undistributed profits and other outside basis differences, different requirements exist depending on whether they involve investments in subsidiaries, in joint ventures or in equity investees.</p> <p>As it relates to investments in domestic subsidiaries, deferred tax liabilities are required on undistributed profits arising after 1992 unless the amounts can be recovered on a tax-free basis and unless the entity anticipates utilizing that method.</p> <p>As it relates to investments in domestic corporate joint ventures, deferred tax liabilities are required on undistributed profits that arose after 1992.</p>	<p>With respect to undistributed profits and other outside basis differences related to investments in subsidiaries, branches and associates, and joint ventures, deferred taxes are recognized except when a parent company (investor or venturer) is able to control the timing of reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.</p>

Impact	US GAAP	IFRS
Deferred taxes on investments in subsidiaries, joint ventures and equity investees (continued)	<p>Deferred taxes are generally recognized on temporary differences related to investments in equity investees.</p> <p>Deferred tax assets for investments in subsidiaries and corporate joint ventures may be recorded only to the extent they will reverse in the foreseeable future.</p>	
Recognition of deferred tax assets The frameworks take differing approaches to the presentation of deferred tax assets. It would be expected that net deferred tax assets recorded would be similar under both standards.	Deferred taxes are recognized in full, but are then reduced by a valuation allowance if it is considered more likely than not that some portion of the deferred taxes will not be realized.	Deferred taxes are recognized when it is considered probable (defined as <i>more likely than not</i>) that sufficient taxable profits will be available to utilize the temporary difference. Valuation allowances are not allowed to be recorded.
Tax rate applied to current and deferred taxes The rate applied when calculating deferred and current taxes may differ depending on the framework used.	US GAAP requires the use of enacted rates when calculating current and deferred taxes.	Current and deferred tax is calculated using enacted or substantively enacted rates.
Exemptions from accounting for temporary differences In certain situations there will be no deferred tax accounting under IFRS that would exist under US GAAP and vice versa.	An exemption exists from the initial recognition of temporary differences in connection with transactions that qualify as leveraged leases under lease-accounting guidance.	<p>An exemption exists in the accounting for deferred taxes from the initial recognition of an asset or liability in a transaction that neither (1) is a business combination nor (2) affects accounting profit or taxable profit/loss at the time of the transaction.</p> <p>No special treatment of leveraged leases exists under IFRS.</p>

Impact	US GAAP	IFRS
<p>Measurement of foreign nonmonetary assets and liabilities where the local currency is not the functional currency</p> <p>The establishment of deferred taxes on exchange rate changes and tax indexing related to nonmonetary assets and liabilities under IFRS is likely to result in additional volatility in the income statement.</p>	<p>No deferred taxes are recognized for differences related to nonmonetary assets and liabilities that are remeasured from local currency into their functional currency by using historical exchange rates (if those differences result from changes in exchange rates or indexing for tax purposes).</p>	<p>Deferred taxes are recognized for the difference between the carrying amount determined by using the historical rate of exchange and the relevant tax basis at the balance sheet date, which may have been affected by exchange rate movements or tax indexing.</p>
<p>Presentation</p> <p>Presentation differences related to deferred taxes could affect the calculation of certain ratios from the face of the balance sheet (including a company's current ratio) because IFRS requires all deferred taxes to be classified as noncurrent.</p>	<p>The classification of deferred tax assets and deferred tax liabilities follows the classification of the related, nontax asset or liability for financial reporting (as either current or noncurrent). If a deferred tax asset or liability is not associated with an underlying asset or liability, it is classified based on the anticipated reversal periods. Any valuation allowances are allocated between current and noncurrent deferred tax assets for a tax jurisdiction on a pro rata basis.</p> <p>The classification of interest and penalties related to uncertain tax positions (either in income tax expense or as a pretax item) represents an accounting policy decision that is to be consistently applied and disclosed.</p>	<p>Generally, deferred tax assets and liabilities are classified net (within individual tax jurisdictions) as noncurrent on the balance sheet. Supplemental note disclosures are included to describe the components of temporary differences as well as the recoverable amount bifurcated between amounts recoverable less than or greater than one year from the balance sheet date.</p> <p>Interest and penalties are to be classified in either interest expense or other operating expenses when they can be clearly identified and separated from the related tax liability.</p>

Impact	US GAAP	IFRS
Tax basis Under IFRS, a single asset or liability may have more than one tax basis, whereas there would generally only be one tax basis per asset or liability under US GAAP.	Tax basis is a question of fact under the tax law. It is determined by the amount that is depreciable for tax purposes as well as the amount that would be deductible upon sale or liquidation of the asset.	Tax basis is based on the expected manner of recovery. Assets and liabilities may have a dual manner of recovery (e.g., through use and through sale). In that case, the carrying amount of the asset or liability is bifurcated, resulting in more than a single temporary difference related to that item.
Interim reporting A worldwide effective tax rate is used to record interim tax provisions under US GAAP. Under IFRS, a separate effective tax rate is used for each jurisdiction.	In general, the interim tax provision is determined by applying the estimated annual worldwide effective tax rate for the consolidated entity to the worldwide consolidated year-to-date pre-tax income.	The interim tax provision is determined by applying an estimated annual effective tax rate to year-to-date pre-tax income. To the extent practicable, a separate estimated average annual effective income tax rate is determined for each taxing jurisdiction and applied individually to the interim period pre-tax income of each jurisdiction.
Technical references		
IFRS	IAS 1, IAS 12, , IAS 34	
US GAAP	ASC 718-740, ASC 740	

Note

The foregoing discussion captures a number of the more significant GAAP differences. It is important to note that the discussion is not inclusive of all GAAP differences in this area.

Recent/proposed guidance

IFRS

In March 2009, the IASB released an exposure draft that proposes changes to its income tax accounting standard. If adopted as proposed, the revised income tax standard would more closely align IFRS and US GAAP in some areas, including: tax basis, presentation, recognition of deferred tax assets, and the deferred tax consequences of investments in other entities (i.e., outside basis differences) in treatment of undistributed profits. In other areas, such as stock-based compensation and intercompany transactions, differences between the two standards will remain. Finally, the revised standard would change the nature of other existing differences in accounting for income tax uncertainties. The exposure draft proposes to eliminate the probable recognition threshold as well as the single best estimate approach. These changes would have a significant impact on the accounting for uncertain tax positions under IFRS (while significant differences to US GAAP would still be present).

Other (e.g., SEC and/or industry highlights)

Further differences in deferred taxes exist between US GAAP and IFRS in the treatment of deferred taxes within share-based payment arrangements. Because those differences represent discrete calculations based on the manner of calculation of the deferred tax asset under both frameworks, the relevant differences have been described in the Expense recognition—share-based payments section of this publication.

Liabilities—other

The guidance in relation to nonfinancial liabilities (e.g., provisions, contingencies and government grants) includes some fundamental differences with potentially significant implications.

For instance, a difference exists in the interpretation of the term *probable*. IFRS defines probable as *more likely than not*, while US GAAP defines probable as *likely to occur*. Because both frameworks reference probable within the liability recognition criteria, the difference could lead companies to record provisions earlier under IFRS than they otherwise would have under US GAAP. The use of the midpoint of a range when several outcomes are equally likely (rather than the low-point estimate, as used in US GAAP) may also lead to increased or earlier expense recognition under IFRS.

As it relates to restructuring provisions, the specific communication to employees that is required prior to the recording of a provision under US GAAP is not required by IFRS. This could lead companies to record restructuring provisions in periods earlier than they previously would have under US GAAP.

The interpretation of probable, as presented in the guidance for contingencies, could again lead to more contingent liabilities being recognized as provisions under IFRS, rather than being disclosed only in the footnotes to a company's financial statements. At the same time, IFRS has a higher threshold for the recognition of reimbursements of recognized losses by requiring that they be virtually certain of realization, where the threshold is lower under US GAAP.

Further details on the foregoing and other selected differences are described in the following table.

Impact	US GAAP	IFRS
Probability and the recognition of provisions Differences in the definition of <i>probable</i> may result in earlier recognition of liabilities under IFRS.	An accrual for a loss contingency is required if it is probable that there is a present obligation resulting from a past event and that an outflow of economic resources is reasonably estimable. Guidance uses the term probable to describe a situation in which the outcome is likely to occur. While a numeric standard for probable does not exist, practice generally considers an event that has a 75 percent or greater likelihood of occurrence to be probable.	A contingent liability is defined as a possible obligation whose outcome will be confirmed only by the occurrence or nonoccurrence of one or more uncertain future events outside the entity's control. A contingent liability becomes a provision and is recorded when three criteria are met: that a present obligation from a past event exists, that the obligation is probable and that a reliable estimate can be made. The term probable is used for describing a situation in which the outcome is more likely than not to occur. Generally, the phrase <i>more likely than not</i> denotes any chance greater than 50 percent.

Impact	US GAAP	IFRS
<p>Measurement of provisions</p> <p>In certain circumstances, the measurement objective of provisions varies under the two frameworks.</p> <p>Significant differences may arise in the selection of the discount rate, particularly in the area of asset retirement obligations.</p> <p>IFRS results in a higher liability being recorded when there is a range of possible outcomes with equal probability.</p>	<p>A single standard does not exist to determine the measurement of obligations. Instead, entities must refer to guidance established for specific obligations (e.g., environmental or restructuring) to determine the appropriate measurement methodology.</p> <p>Pronouncements related to provisions do not necessarily have settlement price or even fair value as an objective in the measurement of liabilities and the guidance often describes an accumulation of the entity's cost estimates.</p> <p>Generally, a provision is discounted only when the timing of the cash flows is fixed or reliably determinable. There are certain instances that meet this criteria (e.g., in the accounting for asset retirement obligations) where discounting is required by the associated guidance.</p> <p>When no amount within a range is a better estimate than any other amount, the low end of the range is accrued.</p>	<p>The amount recognized should be the best estimate of the expenditure required (the amount an entity would rationally pay to settle or transfer to a third party the obligation at the balance sheet date).</p> <p>The anticipated cash flows are discounted using a pre-tax discount rate (or rates) that reflect(s) current market assessments of the time value of money and the risks specific to the liability (for which the cash flow estimates have not been adjusted) if the effect is material. Where there is a continuous range of possible outcomes and each point in that range is as likely as any other, the midpoint of the range is used.</p>

Impact	US GAAP	IFRS
<p>Restructuring provisions (excluding business combinations)</p> <p>Differences exist in the accounting for restructuring or termination benefit provisions (e.g., IFRS does not require specific detailed communication to employees). Reporting under IFRS may alter the timing of expense recognition. Termination benefit costs, for example, may be recognized earlier or later than under US GAAP depending upon the specific facts and circumstances.</p>	<p>The guidance prohibits the recognition of a liability based solely on an entity's commitment to an approved plan.</p> <p>Recognition of a provision for one-time termination benefits requires communication of the details of the plan to employees who could be affected. The communication is to contain sufficient details about the types of benefits so that employees have information for determining the types and amounts of benefits they will receive.</p> <p>Further guidance exists for different types of termination benefits (i.e., special termination benefits, contractual termination benefits, severance benefits and one-time benefit arrangements). For example, one-time termination benefits provided in exchange for an employee's future service are considered a "stay bonus" and are recognized over the employee's future service period.</p> <p>If there is a pre-existing arrangement such that the employer and employees have a mutual understanding of the benefits the employee will receive if involuntarily terminated, the cost of the benefits are accrued when payment is probable and reasonably estimable. In this instance, no announcement to the workforce (nor initiation of the plan) is required prior to expense recognition.</p> <p>Inducements for voluntary terminations are to be recognized when (1) employees accept offers and (2) the amounts can be estimated.</p>	<p>A provision for restructuring costs is recognized when, among other things, an entity has a present obligation.</p> <p>A present obligation exists when, among other conditions, the company is demonstrably committed to the restructuring. A company is usually demonstrably committed when there is legal obligation or when the entity has a detailed formal plan for the restructuring.</p> <p>To record a liability, the company must be unable to withdraw the plan because either it has started to implement the plan or it has announced the plan's main features to those affected (constructive obligation). A current provision is unlikely to be justified if there will be a delay before the restructuring begins or if the restructuring will take an unreasonably long time to complete. As long as an entity is "demonstrably committed" to a plan—for example one which requires future service—a liability would be recognized.</p> <p>Liabilities related to offers for voluntary terminations are recorded when the offer is made to employees and is measured based on the number of employees expected to accept the offer.</p>

Impact	US GAAP	IFRS
Onerous contracts Onerous contract provisions may be recognized earlier and in different amounts under IFRS.	<p>Provisions are not recognized for unfavorable contracts unless the entity has ceased using the rights under the contract (i.e., the cease-use date).</p> <p>One of the most common examples of an unfavorable contract has to do with leased property that is no longer in use. With respect to such leased property, estimated sublease rentals are to be considered in a measurement of the provision to the extent such rentals could reasonably be obtained for the property, even if it is not management's intent to sublease or if the lease terms prohibit subleasing. Incremental expense in either instance is recognized as incurred.</p> <p>US GAAP generally does not allow the recognition of losses on executory contracts prior to such costs being incurred.</p>	<p>Provisions are recognized when a contract becomes onerous regardless of whether the entity has ceased using the rights under the contract.</p> <p>When an entity commits to a plan to exit a lease property, sublease rentals are considered in the measurement of an onerous lease provision only if management has the right to sublease and such sublease income is probable.</p> <p>IFRS generally requires recognition of an onerous loss for executory contracts if the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.</p>

Impact	US GAAP	IFRS
<p>Accounting for government grants</p> <p>IFRS permits the recognition of government grants once there is reasonable assurance that requisite conditions will be met, rather than waiting for the conditions to be fulfilled, as is usually the case under US GAAP. As a result, government grants may be recognized earlier under IFRS.</p>	<p>If conditions are attached to the grant, recognition of the grant is delayed until such conditions have been fulfilled. Contributions of long-lived assets or for the purchase of long-lived assets are to be credited to income over the expected useful life of the asset for which the grant was received.</p>	<p>Government grants are recognized once there is reasonable assurance that both (1) the conditions for their receipt will be met and (2) the grant will be received. Revenue-based grants are deferred in the balance sheet and released to the income statement to match the related expenditure that they are intended to compensate. Capital-based grants are deferred and matched with the depreciation on the asset for which the grant arises.</p> <p>Grants that involve recognized assets are presented in the balance sheet either as deferred income or by deducting the grant in arriving at the asset's carrying amount, in which case the grant is recognized as a reduction of depreciation.</p>

Impact	US GAAP	IFRS
<p>Reimbursements and contingent assets</p> <p>Guidance varies with respect to when these amounts should be recognized. As such, recognition timing differences could arise.</p>	<p>Recovery of recognized losses—an asset relating to the recovery of a recognized loss shall be recognized when realization of the claim for recovery is deemed probable.</p> <p>Recoveries representing gain contingencies—gain contingencies should not be recognized prior to their realization. In certain situations a gain contingency may be considered realized or realizable prior to the receipt of cash.</p>	<p>Reimbursements—where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement shall be recognized when, and only when, it is virtually certain that reimbursement will be received if the entity settles the obligation. The amount recognized for the reimbursement shall be treated as a separate asset and shall not exceed the amount of the provision.</p> <p>The virtually certain threshold may, in certain situations, be achieved in advance of the receipt of cash.</p> <p>Contingent assets—contingent assets are not recognized in financial statements since this may result in the recognition of income that may never be realized. However, when the realization of income is virtually certain, then the related asset is not a contingent asset and its recognition is appropriate.</p>

Technical references

IFRS IAS 20, IAS 37

US GAAP ASC 410-20, ASC 410-30, ASC 420, ASC 450-10, ASC 450-20, ASC 460-10, ASC 944-40, ASC 958-605

Note

The foregoing discussion captures a number of the more significant GAAP differences. It is important to note that the discussion is not inclusive of all GAAP differences in this area.

Recent/proposed guidance

The IASB is currently working on a project to amend IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*. The main objectives of the amendments are (a) convergence with US GAAP in certain areas and (b) improvements in the requirements relating to identification and recognition of liabilities. The Board is proposing to align application guidance for costs associated with restructuring in IAS 37 (and termination benefits in IAS 19 *Employee Benefits*) with the guidance in ASC 420, *Exit or Disposal Cost Obligations*. While it is expected that the amendments would largely align the recognition principles under IFRS and US GAAP in this area, certain other significant differences are expected to remain. The IASB expects to issue a final standard in the second half of 2009.

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Financial liabilities and equity

Financial liabilities and equity

Both US GAAP and IFRS define financial liabilities and require that financing instruments be assessed to determine whether or not they meet the definition of and require treatment as liabilities. In very general terms, financial instruments that do not meet the definition of a liability are classified as equity. The US GAAP definitions of what qualifies as or requires treatment as a liability are narrower than the IFRS definitions. The narrower US GAAP definitions of what requires liability classification result in more instruments being treated as equity/mezzanine equity under US GAAP and comparatively more instruments being treated as liabilities under IFRS.

Under IFRS, contingent settlement provisions and puttable instruments are more likely to result in liability classification. When assessing contingent settlement provisions, IFRS focuses on whether or not the issuer of an instrument has the unconditional right to avoid delivering cash or another financial asset in any or all potential outcomes. The fact that the contingency associated with the settlement provision might not be triggered does not influence the analysis unless the contingency is not genuine or it arises only upon liquidation. With very limited exceptions, puttable instruments are financial liabilities under IFRS.

US GAAP examines whether or not the instrument in question contains an unconditional redemption requirement. Unconditional redemption requirements result in liability classification. Contingent settlement/redemption requirements and/or put options, however, would generally not be unconditional, as they may not occur. As such, under US GAAP liability classification would not be required. SEC-listed entities, however, would need to consider application of mezzanine accounting guidance. When an instrument that qualified for equity treatment under US GAAP is classified as a liability under IFRS there are potential follow-on implications. For example, an entity must consider and address the further potential need to bifurcate and separately account for embedded derivatives within liability-classified host contracts. Also, because balance sheet classification drives the treatment of disbursements associated with such instruments, classification differences may impact earnings (i.e., interest expense calculated by using the effective interest method, as opposed to dividends) as well as key balance sheet ratios.

Under IFRS, if an instrument has both a liability component and an equity component (e.g., redeemable preferred stock with dividends paid solely at the discretion of the issuer), the issuer is required to separately account for each component. The liability component is recognized at fair value calculated by discounting the cash flows associated with the liability component at a market rate for a similar debt host instrument and the equity component is measured as the residual amount. US GAAP generally does not have the concept of compound financial instruments outside of instruments with equity conversion features.

For hybrid instruments that contain conversion options, there are situations where both accounting models call for separate recording of the liability and equity components. Under US GAAP, the form of the instrument's conversion option dictates the manner in which the different components are accounted for.

Bifurcation/split accounting under IFRS versus singular accounting under US GAAP can create a significantly different balance sheet presentation while also impacting earnings (mainly due to recognition of interest expense at the market rate at inception as opposed to any contractual rate within the compound arrangement).

Whether an instrument (freestanding or embedded) that is settled by delivery or receipt of an issuer's own shares is considered equity may be a source of significant differences between IFRS and US GAAP. For example, net share settlement would immediately cause a warrant or an embedded conversion option to fail equity classification under IFRS; under US GAAP, a similar feature would not automatically taint equity classification and further analysis to determine classification would be required. Likewise, a contract with settlement alternatives that includes one that does not result in equity classification (e.g., a choice between gross settlement and net cash settlement) would fail equity classification under IFRS even if the settlement choice resides with the issuer.

There are some significant differences in the treatment of written puts that will be settled by gross receipt of an entity's own shares. Under US GAAP, such items are measured initially and subsequently at fair value. Under IFRS, even though the contract in itself may meet the definition of equity if the contract is for the receipt of a fixed number of the entity's own shares for a fixed amount of cash, IFRS requires the entity to set up a financial liability for the discounted value of the amount of cash it may be required to pay.

Additional differences have to do with financial liabilities that are carried at amortized cost. For these liabilities, both IFRS and US GAAP use the effective interest method to calculate amortized cost and allocate interest expense over the relevant period. The effective interest method is based on the effective interest rate calculated at initial recognition of the financial instrument. Under IFRS the effective interest rate is calculated based on estimated future cash flows through the expected life of the financial instrument. Under US GAAP, the effective interest rate is generally calculated based on the contractual cash flows through the contractual life of the financial liability. Certain exceptions to this rule involve (1) puttable debt (amortized over the period from the date of issuance to the first put date) and (2) callable debt (a policy decision to amortize over either the contractual life or the estimated life). Under IFRS, changes in the estimated cash flow due to a closely related embedded derivative that is not bifurcated result in a cumulative catch-up reflected in the current-period income statement. US GAAP does not have the equivalent of a cumulative-catch-up-based approach.

Further details on the foregoing and other selected differences are described in the following table.

Impact	US GAAP	IFRS
Classification		
<p>Contingent settlement provisions</p> <p>Contingent settlement provisions, such as provisions requiring redemption upon a change in control, result in liability classification under IFRS unless the contingency arises only upon liquidation or is not genuine.</p> <p>Items classified as mezzanine equity under US GAAP generally are classified as liabilities under IFRS.</p>	<p>A contingently redeemable financial instrument (e.g., one redeemable only if there is a change in control) is outside the scope of ASC 480 because its redemption is not unconditional. Any conditional provisions must be assessed to ensure that the contingency is substantive.</p> <p>For SEC-listed companies applying US GAAP, certain types of securities require classification in the mezzanine equity category of the balance sheet. Examples of items requiring mezzanine classification are instruments with contingent settlement provisions or puttable shares as discussed in the Puttable shares section.</p> <p>Mezzanine classification is a US-public-company concept that is also preferred (but not required) for private companies.</p>	<p>IAS 32 notes that a financial instrument may require an entity to deliver cash or another financial asset in the event of the occurrence or nonoccurrence of uncertain future events that are beyond the control of both the issuer and the holder of the instrument. Contingencies may include linkages to such events as a change in control or to other matters such as a change in a stock market index, consumer price index, interest rates, or net income.</p> <p>If the contingency is outside of the issuer's control, the issuer of such an instrument does not have the unconditional right to avoid delivering cash or another financial asset. Therefore, except in limited circumstances (such as if the contingency were not genuine or if it is triggered only in the event of a liquidation of the issuer), instruments with contingent settlement provisions represent liabilities.</p> <p>As referenced previously, the guidance focuses on the issuer's unconditional ability to avoid settlement no matter what contingencies may or may not be triggered.</p> <p>There is no concept of mezzanine classification under IFRS.</p>

Impact	US GAAP	IFRS
<p>Derivative on own shares—“fixed for fixed” versus indexed to issuer’s own shares</p> <p>When determining issuer’s classification of a derivative on its own shares, IFRS looks at whether the equity derivative meets a “fixed for fixed” requirement while US GAAP uses a two step model. Although Step 2 of the US GAAP model uses a similar “fixed for fixed” concept, the application of the concept, differs significantly between US GAAP and IFRS.</p> <p>These differences can impact classification as equity or a derivative asset or liability (with derivative classification more common under IFRS).</p>	<p>Equity derivatives need to be indexed to the issuer’s own shares to be classified as equity. The assessment follows a two step approach under ASC 815-40-15.</p> <p>Step 1 considers where there are any contingent exercise provisions and, if so, they cannot be based on an observable market or index other than those referenced to the issuer’s own shares or operations.</p> <p>Step 2 considers the settlement amount. Only settlement amounts equal to the difference between the fair value of a fixed number of the entity’s equity shares and a fixed monetary amount, or a fixed amount of a debt instrument issued by the entity, will qualify for equity classification.</p> <p>If the instrument’s strike price (or the number of shares used to calculate the settlement amount) is not fixed as outlined above, the instrument may still meet the equity classification criteria; this could occur where the variables that might effect settlement include inputs to the fair value of a “fixed for fixed” forward or option on equity shares and the instrument does not contain a leverage factor.</p>	<p>Only contracts that provide for gross physical settlement meet the fixed-for-fixed criteria (i.e., a fixed number of shares for a fixed amount of cash) and can be classified as equity. Variability in the amount of cash or the number of shares to be delivered results in financial liability classification.</p> <p>For example, a warrant issued by Company X has a strike price adjustment based on the movements in Company X’s stock price. This feature would fail the fixed-for-fixed criteria under IFRS—the same adjustment would meet the fixed-for-fixed criteria under US GAAP. As such, for Company X’s accounting for the warrant, IFRS would result in liability classification, whereas US GAAP would result in equity classification.</p>

Impact	US GAAP	IFRS
<p>Derivatives on own shares—settlement models</p> <p>Entities will need to consider how derivative contracts on an entity's own shares will be settled. Many of these contracts that are classified as equity under US GAAP (e.g., warrants that will be net share settled or those where the issuer has settlement options) will be classified as derivatives under IFRS. Derivative classification will create additional volatility in the income statement.</p>	<p>Derivative contracts that are in the scope of ASC 815-40 and that:</p> <ol style="list-style-type: none"> 1. require physical settlement or net share settlement; and 2. give the issuer a choice of net cash settlement or settlement in its own shares <p>are considered equity instruments, provided they meet the criteria set forth within the literature.</p> <p>Analysis of a contract's terms is necessary to determine whether the contract meets the qualifying criteria, some of which can be difficult to meet in practice.</p> <p>Similar to IFRS, derivative contracts that require net cash settlement are assets or liabilities and contracts that require settlement in shares are equity instruments.</p> <p>Contracts that give the counterparty a choice of net cash settlement or settlement in shares (physical or net settlement) result in derivative classification. However, if the issuer has a choice of net cash settlement or share settlement, the contract can still be considered an equity instrument.</p>	<p>Contracts that are net settled (net cash or net shares) are classified as liabilities or assets. This is also the case even if the settlement method is at the issuer's discretion.</p> <p>Gross physical settlement is required to achieve equity classification.</p> <p>Unlike US GAAP, under IFRS, a derivative contract that gives one party (either the holder or the issuer) a choice over how it is settled (net in cash, net in shares or by gross delivery) is a derivative asset/liability unless all of the settlement alternatives would result in the contract being an equity instrument.</p>

Impact	US GAAP	IFRS
<p>Written put option on the issuer's own shares</p> <p>Written puts that are to be settled by gross receipt of the entity's own shares are treated as derivatives under US GAAP, while IFRS requires the entity to set up a liability for the discounted value of the amount of cash the entity may be required to pay.</p>	<p>A financial instrument—other than an outstanding share—that at inception (1) embodies an obligation to repurchase the issuer's equity shares or is indexed to such an obligation and (2) requires or may require the issuer to settle the obligation by transferring assets shall be classified as a liability (or an asset in some circumstances). Examples include forward purchase contracts or written put options on the issuer's equity shares that are to be physically settled or net cash settled.</p> <p>ASC 480 requires written put options to be measured at fair value, with changes in fair value recognized in current earnings.</p>	<p>If the contract meets the definition of an equity instrument (because it requires the entity to purchase a fixed amount of its own shares for a fixed amount of cash), any premium received or paid must be recorded in equity. Therefore, the premium received on such a written put is classified as equity (whereas under US GAAP, the fair value of the written put is recorded as a liability).</p> <p>In addition, when an entity has an obligation to purchase its own shares for cash (e.g., under a forward contract to purchase its own shares or under a written put), the issuer records a financial liability for the discounted value of the amount of cash that the entity may be required to pay. The liability is recorded against equity.</p>

Impact	US GAAP	IFRS
<p>Compound instruments that are not convertible instruments (that do not contain equity conversion features)</p> <p>Bifurcation and split accounting under IFRS may result in significantly different treatment, including increased interest expense.</p>	<p>The guidance does not have the concept of compound financial instruments outside of instruments with equity conversion features. As such, under US GAAP the instrument would be classified wholly within liabilities or equity.</p>	<p>If an instrument has both a liability component and an equity component—known as a compound instrument (e.g., redeemable preferred stock with dividends paid solely at the discretion of the issuer)—IFRS requires separate accounting for each component of the compound instrument.</p> <p>The liability component is recognized at fair value calculated by discounting the cash flows associated with the liability component at a market rate for a similar debt host instrument, and the equity component is measured as the residual amount.</p> <p>The accretion calculated in the application of the effective interest rate method on the liability component is classified as interest expense.</p>
<p>Convertible instruments (compound instruments that contain equity conversion features)</p> <p>Differences in how and when convertible instruments get bifurcated and/or how the bifurcated portions get measured can drive substantially different results.</p>	<p>Equity conversion features should be separated from the liability host and recorded separately as embedded derivatives only if they meet certain criteria (e.g., fail to meet the scope exception of ASC 815).</p>	<p>For convertible instruments with a conversion feature characterized by a fixed amount of cash for a fixed number of shares, IFRS requires bifurcation and split accounting between the liability and equity components of the instrument.</p>

Impact	US GAAP	IFRS
Convertible instruments (compound instruments that contain equity conversion features) (continued)	<p>If the conversion feature is not recorded separately, then the entire convertible instrument may be considered one unit of account—interest expense would reflect cash interest if issued at par. However, there are a few exceptions:</p> <ul style="list-style-type: none"> • For convertible debt instruments that may be settled in cash, the liability and equity components of the instrument should be separately accounted for by allocating the proceeds from the issuance of the instrument between the liability component and the embedded conversion option (i.e., the equity component). This allocation is done by first determining the carrying amount of the liability component based on the fair value of a similar liability excluding the embedded conversion option and then allocating to the embedded conversion option the excess of the initial proceeds ascribed to the convertible debt instrument over the amount allocated to the liability component. • A convertible debt may contain a beneficial conversion feature (BCF) when the strike price on the conversion option is “in the money.” The BCF is generally recognized and measured by allocating a portion of the proceeds received, equal to the intrinsic value of the conversion feature, to equity. 	<p>The liability component is recognized at fair value calculated by discounting the cash flows associated with the liability component—at a market rate for nonconvertible debt—and the equity conversion feature is measured as the residual amount and recognized in equity with no subsequent remeasurement.</p> <p>Equity conversion features within liability host instruments that fail the fixed-for-fixed requirement are considered to be embedded derivatives. Such embedded derivatives are bifurcated from the host debt contract and measured at fair value, with changes in fair value recognized in the income statement.</p> <p>IFRS does not have a concept of BCF as the compound instruments are already accounted for based on their components.</p>

Impact	US GAAP	IFRS
<p>Puttable shares/redeemable upon liquidation</p> <p>Puttable shares</p> <p>Puttable shares are more likely to be classified as liabilities under IFRS.</p> <p>The potential need to classify certain interests in open-ended mutual funds, unit trusts, partnerships and the like as liabilities under IFRS could lead to situations where some entities have no equity capital in their financial statements.</p>	<p>Puttable shares</p> <p>The redemption of puttable shares is conditional upon the holder exercising the put option. This contingency removes puttable shares from the scope of instruments that ASC 480 requires to be classified as a liability.</p> <p>As discussed for contingently redeemable instruments, SEC registrants would classify these instruments as “mezzanine” while such classification is encouraged, but not required, for private companies.</p>	<p>Puttable shares</p> <p>Puttable instruments are generally classified as financial liabilities because the issuer does not have the unconditional right to avoid delivering cash or other financial assets. Under IFRS, the legal form of an instrument (i.e., as debt or equity) does not necessarily influence the classification of a particular instrument.</p> <p>Under this principle, IFRS may require certain interests in open-ended mutual funds, unit trusts, partnerships and the like to be classified as liabilities (since holders can require cash settlement). This could lead to situations where some entities have no equity capital in their financial statements.</p> <p>An entity may classify certain puttable instrument as equity, provided they have particular features and meet certain specific conditions in IAS 32.</p>

Impact	US GAAP	IFRS
<p>Puttable shares/redeemable upon liquidation (continued)</p> <p>Redeemable upon liquidation</p> <p>Differences with respect to the presentation of these financial instruments issued by a subsidiary in the parents consolidated financial statements can drive substantially different results.</p>	<p>Redeemable upon liquidation</p> <p>ASC 480 scopes out instruments that are only redeemable upon liquidation. Therefore, such instruments may achieve equity classification for finite-lived entities.</p> <p>In classifying these financial instruments issued by a subsidiary in a parent's consolidated financial statements, US GAAP permits an entity to defer the application of ASC 480; the result is that the redeemable interests issued by a subsidiary is not a liability in the parent's consolidated financial statements</p>	<p>Redeemable upon liquidation</p> <p>For instruments issued out of finite-lived entities that are redeemable upon liquidation, equity classification may be appropriate if certain conditions are met. However, when classifying redeemable financial instruments issued by a subsidiary (either puttable or redeemable upon liquidation) for a parent's consolidated accounts, equity classification at the subsidiary level is not extended to the parent's classification of the redeemable noncontrolling interests in the consolidated financial statements as the same instrument would not meet the specific IAS 32 criteria from the parent's perspective.</p>
Measurement		
<p>Initial measurement of a liability with a related party</p> <p>There are fundamental differences in the approach to related-party liabilities under the two accounting models that may impact the values at which these liabilities are initially recorded. The IFRS model may, in practice, be more challenging to implement.</p>	<p>When an instrument is issued to a related party at off-market terms, one should consider which model the instrument falls within the scope of as well as the facts and circumstances of the transaction (i.e., the existence of unstated rights and privileges) in determining how the transaction should be recorded. There is, however, no requirement to initially record the transaction at fair value.</p> <p>The ASC 850 presumption that related party transactions are not at arm's length and the associated disclosure requirements should also be considered.</p>	<p>When an instrument is issued to a related party, the liability should initially be recorded at fair value, which may not be the value of the consideration received. The difference between fair value and the consideration received (i.e., any additional amount lent or borrowed) is accounted for as a current-period expense, income, or as a capital transaction based on its substance</p>

Impact	US GAAP	IFRS
<p>Effective-interest-rate calculation</p> <p>Differences between the expected lives and the contractual lives of financial liabilities have different implications under the two frameworks unless the instruments in question are carried at fair value. The difference in where the two accounting frameworks place their emphasis (contractual term for US GAAP and expected outcome for IFRS) can impact carrying values and the timing of expense recognition.</p> <p>Similarly, differences in how revisions to estimates get treated also impact carrying values and expense recognition timing, with the potential for greater volatility under IFRS.</p>	<p>The effective interest rate used for calculating amortization under the effective interest method generally discounts contractual cash flows through the contractual life of the instrument. However, there may be circumstances where expected life is used.</p>	<p>The effective interest rate used for calculating amortization under the effective interest method discounts estimated cash flows through the expected—not the contractual—life of the instrument.</p> <p>Generally, if the entity revises its estimate after initial recognition, the carrying amount of the financial liability should be revised to reflect actual and revised estimated cash flows at the original effective interest rate, with a cumulative-catch-up adjustment being recorded in profit and loss. Revisions of the estimated life or of the estimated future cash flows may exist, for example, in connection with debt instruments that contain a put or call option that does not need to be bifurcated or whose coupon payments vary. Payments may vary because of an embedded feature that does not meet the definition of a derivative because its underlying is a nonfinancial variable specific to a party to the contract (e.g., cash flows that are linked to earnings before interest, taxes, depreciation and amortization; sales volume; or the earnings of one party to the contract).</p> <p>Generally, floating rate instruments (e.g., LIBOR plus spread) issued at par are not subject to the cumulative catch-up approach; rather, the effective interest rate is revised as market rates change.</p>

Impact	US GAAP	IFRS
Transaction costs (also known as debt issue costs) When applicable, the balance sheet presentation of transaction costs (separate asset versus a component of the instrument's carrying value) differs under the two standards. IFRS prohibits the balance sheet gross up required by US GAAP.	When the liability is not carried at fair value through income, transaction costs are deferred as an asset. Transaction costs are expensed immediately when the liability is carried at fair value, with changes recognized in profit and loss.	When the liability is not carried at fair value through income, transaction costs are deducted from the carrying value of the financial liability and are not recorded as separate assets. Rather, they are accounted for as a debt discount and amortized using the effective interest method. Transaction costs are expensed immediately when the liability is carried at fair value, with changes recognized in profit and loss.
Technical references		
IFRS	IAS 32, IAS 39, IFRIC 2	
US GAAP	ASC 470-20, ASC 470-20-25-12, ASC 480, ASC 480-10-65-1, ASC 815, ASC 815-15-25-4 through 25-5, ASC 815, ASC 815-40, ASC 815-40-25, ASC 825, ASC 850, ASC 860, CON 6, ASR 268	

Note

The foregoing discussion captures a number of the more significant GAAP differences. It is important to note that the discussion is not inclusive of all GAAP differences in this area.

Recent/proposed guidance

FASB and IASB Comment requests on *Financial Instruments with Characteristics of Equity*

In November 2007 and February 2008, the FASB and the IASB, respectively, issued their *Preliminary Views on Financial Instruments with Characteristics of Equity*. Both boards received comments back during 2008. The Boards have indicated their intent to use input received to their individual requests as the basis of a joint project to develop a high-quality common standard. The intent of the projects is to reduce complexity and inconsistent results in application and is likely to result in more instruments being classified as liabilities, which could increase earnings volatility and/or impact financial statement metrics and debt covenants. The Boards are currently refining the approach based upon feedback received and are expected to release an exposure draft in early 2010 with a final standard no earlier than 2011.

Financial Instruments: Replacement of IAS 39

In March 2008 the IASB released a discussion paper that discusses the main causes of complexity in reporting financial instruments. It also discusses possible intermediate and long-term approaches to improving financial reporting and reducing complexity. The IASB has noted that many preparers of financial statements, their auditors and users of financial statements find the requirements for reporting financial instruments complex. The IASB and the FASB have been urged by many to develop new standards of financial reporting for financial instruments that are principles-based and less complex than today's requirements.

As a result of the financial crisis, work on this project was accelerated to change the accounting for financial instruments. The replacement of IAS 39 project is being broken down into three stages, (1) classification and measurement of financial assets and liabilities, (2) impairment and (3) hedge accounting. The IASB is expected to release exposures drafts over the remainder of 2009 with classification and measurement already released in July 2009, impairment in October 2009, and hedge accounting in December 2009, with final standards in time for year-end financial statements for 2009 (classification and measurement) and during 2010 (impairment and hedge accounting). The classification and measurement project is expected to eliminate the requirement to evaluate embedded derivatives in financial instruments.

This project has the potential to create significant differences when compared to current US GAAP. However, both the IASB and FASB are coordinating efforts in their projects to reduce complexity in reporting financial instruments, although the ultimate standards may not be fully converged.

Credit Risk in Liability Measurement

In June 2009, the IASB published a discussion paper on the use of credit risk in liability measurement. The discussion paper was accompanied by a staff paper that outlined the three most often-cited arguments in favor of including credit risk in current measurement of liabilities and the three most often-cited arguments against it. The objective of the discussion paper is to generate a focused discussion that will enhance the debate on this topic that has generated more comment and controversy than any other issue in fair value.

The comment period on the discussion paper ended on September 1, 2009.

ASC 815-40-15, Determining Whether an Instrument (or Embedded Feature) Is Indexed to an Entity's Own Stock

This guidance addresses the determination of whether an equity-linked financial instrument (or embedded feature) is indexed to an entity's own stock, which is an important consideration in determining the instrument's accounting classification. The guidance requires companies to apply a two-step approach, separately evaluating the instrument's contingent exercise provisions and then the instrument's settlement provisions. Certain common price protection provisions may result in some instruments (or embedded features) being reclassified to assets or liabilities (or bifurcated) and marked-to-market through earnings. The guidance is applicable to existing instruments and is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. Refer to the detailed point above titled "Derivative on own shares—'fixed for fixed' versus indexed to issuer's own shares."

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Derivatives and hedging

Derivatives and hedging

Derivatives and hedging represent one of the more complex and nuanced topical areas within both US GAAP and IFRS. While IFRS is generally viewed as less rules laden than US GAAP, the difference is less dramatic in relation to derivatives and hedging wherein both frameworks embody a significant volume of detailed implementation guidance.

In the area of derivatives and embedded derivatives, the IFRS definition of derivatives is broader than that under US GAAP; therefore, more instruments may be required to be accounted for at fair value through the income statement under IFRS. On the other hand, the application of the scope exception around “own use”/“normal purchase normal sale” may result in fewer derivative contracts at fair value under IFRS as these are scoped out of IFRS while elective under US GAAP. Also, there are differences in the identification of embedded derivatives within financial and nonfinancial host contracts that should be carefully considered. In terms of measurement of derivatives, day one gains or losses cannot be recognized under IFRS unless supported by appropriate observable current market transactions or if all of the inputs into the valuation model used to derive the day one difference are observable. Under US GAAP, day one gains and losses, where fair value is derived from unobservable inputs, are permitted.

Although the hedging models under IFRS and US GAAP are founded on similar principles, there are a number of application differences. Some of the differences result in IFRS being more restrictive than US GAAP, whereas other differences provide more flexibility under IFRS.

Areas where IFRS is more restrictive than US GAAP include the nature, frequency and methods of measuring and assessing hedge effectiveness. As an example, US GAAP provides for a shortcut method that allows an entity to assume no ineffectiveness and, hence, bypass an effectiveness test as well as the need to measure quantitatively the amount of hedge ineffectiveness. The US GAAP shortcut method is available only for certain fair value or cash flow hedges of interest rate risk using interest rate swaps (when certain stringent criteria are met). IFRS has no shortcut method equivalent. To the contrary, IFRS requires that, in all instances, hedge effectiveness be measured and any ineffectiveness be recorded in profit or loss. IFRS does acknowledge that in certain situations little or no ineffectiveness could arise, but IFRS does not provide an avenue whereby an entity may assume no ineffectiveness.

Because the shortcut method is not accepted under IFRS, companies utilizing the shortcut method under US GAAP will need to prepare the appropriate level of IFRS-compliant documentation if they want to maintain hedge accounting. The documentation will need to be in place no later than at the transition date to IFRS if hedge accounting is to be maintained on an uninterrupted basis. For example, for a company whose first IFRS-based financial statements will be issued for the three years ended December 31, 2012, hedging documentation needs to be in place as of the opening balance sheet date. Hence, documentation needs to be in place as of January 1, 2010, if the entity wants to continue to apply hedge accounting on an uninterrupted basis.

Another area where IFRS is more restrictive involves the use of purchased options as a hedging instrument. Under IFRS, when hedging one-sided risk in a forecasted transaction under a cash flow hedge (e.g., for foreign currency or price risk), only the intrinsic value of a purchased option is deemed to reflect the one-sided risk of the hedged item. As a result, for hedge relationships where the critical terms of the purchased option match the hedged risk, generally, the change in intrinsic value will be deferred in equity while the change in time value will be recorded in the income statement. However, US GAAP permits an entity to assess effectiveness based on the entire change in fair value of the purchased option. There is also less flexibility, under IFRS, in the accounting for and hedging of servicing rights.

IFRS is also more restrictive than US GAAP in relation to the use of internal derivatives. Restrictions under the IFRS guidance may necessitate that entities desiring hedge accounting enter into separate, third-party hedging instruments for the gross amount of foreign currency exposures in a single currency, rather than on a net basis (as is done by many treasury centers under US GAAP).

At the same time, there are a number of areas where IFRS provides opportunities not available under US GAAP. Such opportunities arise in a series of areas where hedge accounting can be accomplished under IFRS, whereas it would have been precluded under US GAAP. For example, under IFRS an entity can achieve hedge accounting in relation to the foreign currency risk associated with a firm commitment to acquire a business in a business combination (whereas US GAAP would not permit hedge accounting). At the same time, IFRS allows an entity to utilize a single hedging instrument to hedge more than one risk in two or more hedged items (this designation is precluded under US GAAP). That difference may allow entities under IFRS to adopt new and sometimes more complex risk management strategies while still achieving hedge accounting. IFRS is more flexible than US GAAP with respect to the ability to achieve fair value hedge accounting in relation to interest rate risk within a portfolio of dissimilar financial assets and in relation to hedging a portion of a specified risk and/or a portion of a time period to maturity (i.e., partial-term hedging) of a given instrument to be hedged. A series of further differences exists as well.

As companies work to understand and embrace the new opportunities and challenges associated with adopting IFRS in this area, it is important that they ensure that data requirements and underlying systems support are fully considered.

Further details on the foregoing and other selected differences are described in the following table.

Impact	US GAAP	IFRS
Derivative definition and scope		
Net settlement provisions More instruments will qualify as derivatives under IFRS. Some instruments, such as option and forward agreements to buy unlisted equity investments, are accounted for as derivatives under IFRS, but not under US GAAP.	To meet the definition of a derivative, a financial instrument or other contract must require or permit net settlement. US GAAP generally excludes from the scope of ASC 815 certain instruments linked to unlisted equity securities when such instruments fail the net settlement requirement and are therefore not accounted for as derivatives. An option contract between an acquirer and a seller to buy or sell stock of an acquiree at a future date that results in a business combination may not meet the definition of a derivative as it may fail the net settlement requirement (e.g., the acquiree's shares are not listed so the shares may not be readily convertible to cash).	IFRS does not include a requirement for net settlement within the definition of a derivative. There is an exception under IAS 39 for derivatives whose fair value cannot be measured reliably (i.e., instruments linked to equity instruments that are not reliably measurable), which could result in not having to account for such instruments at fair value. In practice, however, this exemption is very narrow in scope because in most situations it is expected that fair value can be measured reliably even for unlisted securities. Effective January 1, 2010, an option contract between an acquirer and a seller to buy or sell stock of an acquiree at a future date that results in a business combination would be considered a derivative under IAS 39 for the acquirer; however, the option may be classified as equity from the seller's perspective.
Own use versus normal purchase normal sale (NPNS) The "own use" exception is mandatory under IFRS while the "normal purchase normal sale" exception is elective under US GAAP.	There are many factors to consider in determining whether a contract related to nonfinancial items can qualify for the NPNS exception. If a contract meets the requirement of the NPNS exception, then the reporting entity must document that it qualifies in order to apply the NPNS exception—otherwise, it will be considered a derivative.	Similar to US GAAP, there are many factors to consider in determining whether a contract related to nonfinancial items qualifies for the "own use" exception. While US GAAP requires documentation to apply the NPNS exception (i.e., it is elective), IFRS requires a contract to be accounted for as own use (i.e., not accounted for as a derivative) if the own use criteria are satisfied.

Impact	US GAAP	IFRS
Embedded derivatives		
Reassessment of embedded derivatives Differences with respect to the reassessment of embedded derivatives may result in significantly different outcomes under the two frameworks. Generally, reassessment is more frequent under US GAAP.	<p>If a hybrid instrument contains an embedded derivative that is not clearly and closely related at inception, and it is not bifurcated (because it does not meet the definition of a derivative), it must be continually reassessed to determine whether bifurcation is required at a later date. Once it meets the definition of a derivative, the embedded derivative is bifurcated and measured at fair value with changes in fair value recognized in earnings.</p> <p>Similarly, the embedded derivative in a hybrid instrument that is not clearly and closely related at inception and is bifurcated must also be continually reassessed to determine whether it subsequently fails to meet the definition of a derivative. Such an embedded derivative should cease to be bifurcated at the point at which it fails to meet the requirements for bifurcation.</p> <p>An embedded derivative that is clearly and closely related is not reassessed subsequent to inception for the “clearly and closely related” feature. However, for nonfinancial host contracts, the assessment of whether an embedded foreign currency derivatives is clearly and closely related to the host contract should only be performed at inception of the contract.</p>	<p>IFRS precludes reassessment of embedded derivatives after inception of the contract unless there is a change in the terms of the contract that significantly modifies the expected future cash flows that would otherwise be required under the contract.</p> <p>Having said that, if an entity reclassifies a financial asset out of the held for trading category, embedded derivatives must be assessed and, if necessary, bifurcated.</p>

Impact	US GAAP	IFRS
<p>Calls and puts in debt instruments</p> <p>IFRS and US GAAP have fundamentally different approaches to assessing whether puts and calls embedded in debt host instruments require bifurcation.</p>	<p>Multiple tests are required in evaluating whether an embedded call or put is clearly and closely related to the debt host. The failure of one or both of the below outlined tests is common and typically results in the need for bifurcation.</p> <p>Test 1—If a debt instrument is issued at a substantial premium or discount and a contingent call or put can accelerate repayment of principal, then the call or put is not clearly and closely related.</p> <p>Test 2—If there is no contingent call or put that can accelerate principal or if the debt instrument is not issued at a substantial premium or discount, then it must be assessed whether the debt instrument can be settled in such a way that the holder would not recover substantially all of its recorded investments or the embedded derivative would at least double the holder's initial return and the resulting rate would be double the then current market rate of return. However, this rule is subject to certain exceptions.</p>	<p>Calls, puts or prepayment options embedded in a hybrid instrument are closely related to the debt host instrument if either: a) the exercise price approximates the amortized cost on each exercise date or b) the exercise price of a prepayment option reimburses the lender for an amount up to the approximate present value of the lost interest for the remaining term of the host contract. Once determined to be closely related as outlined above, these items do not require bifurcation.</p>

Impact	US GAAP	IFRS
<p>Nonfinancial host contracts—currencies commonly used</p> <p>Although IFRS and US GAAP have similar guidance in determining when to separate foreign currency embedded derivatives in a nonfinancial host, there is more flexibility under IFRS in determining that the currency is closely related.</p>	<p>US GAAP requires bifurcation of a foreign currency embedded derivative from a nonfinancial host unless the payment is:</p> <ol style="list-style-type: none"> 1. denominated in the local currency or functional currency of a substantial party to the contract; 2. the price is routinely denominated in that foreign currency in international commerce (e.g., US dollar for crude oil transactions); or 3. a foreign currency used because a party operates in a hyperinflationary environment. 	<p>Criteria (a) and (b) cited for US GAAP are also in IFRS. However, bifurcation of a foreign currency embedded derivative from a nonfinancial host is not required if payments are denominated in a currency that is commonly used to purchase or sell such items in the economic environment in which the transaction takes place.</p> <p>For example, Company X, in Russia (functional currency and local currency is Russian ruble) that sells timber to another Russian company (with a ruble functional currency) in euros. Since the euro is a currency commonly used in Russia, bifurcation of a foreign currency embedded derivative from the nonfinancial host contract would not be required under IFRS.</p>
<p>Embedded credit derivatives in synthetic collateralized debt obligations (CDOs)</p> <p>Bifurcation of embedded credit derivatives from synthetic CDOs under IFRS can drive significantly more income statement volatility compared to that under US GAAP.</p>	<p>US GAAP does not consider a synthetic CDO to have an embedded credit derivative that is required to be bifurcated. Therefore, an investor in such instruments generally accounts for the investment as one unit of account.</p>	<p>The embedded credit derivative in synthetic CDOs is considered not to be closely related to the debt host contract and requires bifurcation. This is because the issuer (typically a special purpose entity) transfers the credit risk of an asset it does not own by writing a credit default swap (while the SPE usually owns treasuries or other highly rated securities).</p>

Impact	US GAAP	IFRS
Measurement of derivatives		
Day one gains and losses		
<p>Day one gains and losses occur when the entity uses a model to measure the fair value of the instrument and the model price at initial recognition is different from the transaction price.</p> <p>The ability to recognize day one gains and losses is different under both frameworks with gain/loss recognition more common under US GAAP.</p>		
	<p>In some circumstances, the transaction price is not equal to fair value, usually when the market in which the transaction occurs differs from the market where the reporting entity could transact. For example, banks can access wholesale and retail markets—the wholesale price may result in a day one gain compared to the transaction price in the retail market.</p> <p>In these cases, entities must recognize day one gains and losses even if some inputs to the measurement model are not observable.</p>	<p>Day one gains and losses are recognized only when the fair value is evidenced by comparison with other observable current market transactions in the same instrument or is based on a valuation technique whose variables include only data from observable markets.</p>
Hedge qualifying criteria		
When to assess effectiveness		
<p>Non-SEC-listed entities may see greater flexibility in the frequency of required effectiveness testing under IFRS.</p> <p>Although the rules under IFRS allow less frequent effectiveness testing in certain situations, SEC-listed entities will still be required to assess effectiveness on a quarterly basis in conjunction with their interim reporting requirements.</p>		
	<p>US GAAP requires that hedge effectiveness be assessed whenever financial statements or earnings are reported and at least every three months (regardless of how often financial statements are prepared).</p>	<p>IFRS requires that hedges be assessed for effectiveness on an ongoing basis and that effectiveness be measured, at a minimum, at the time an entity prepares its annual or interim financial reports.</p> <p>Therefore, if an entity is required to produce only annual financial statements, IFRS requires that effectiveness be tested only once a year. An entity may, of course, choose to test effectiveness more frequently.</p>

Impact	US GAAP	IFRS
Hedge accounting practices allowed under US GAAP that are not acceptable under IFRS		
<p>Effectiveness testing and measurement of hedge ineffectiveness</p> <p>IFRS requires an increased level of hedge effectiveness testing and/or detailed measurement than is required under US GAAP.</p> <p>There are a number of similarities between the effectiveness-testing methods that are acceptable under US GAAP and those that are acceptable under IFRS. At the same time, important differences exist in areas such as the use of the shortcut method and the matched-terms method.</p>	<p>US GAAP does not specify a single method for assessing hedge effectiveness prospectively or retrospectively. The method an entity adopts depends on the entity's risk management strategy and is included in the documentation prepared at the inception of the hedge.</p>	<p>IFRS does not specify a single method for assessing hedge effectiveness prospectively or retrospectively. The method an entity adopts depends on the entity's risk management strategy and is included in the documentation prepared at the inception of the hedge. The most common methods used are the critical-terms comparison, the dollar-offset method and regression analysis.</p>

Impact	US GAAP	IFRS
Effectiveness testing and measurement of hedge ineffectiveness (continued)	<p>Shortcut method</p> <p>US GAAP provides for a shortcut method that allows an entity to assume no ineffectiveness (and, hence, bypass an effectiveness test) for certain fair value or cash flow hedges of interest rate risk using interest rate swaps (when certain stringent criteria are met).</p> <p>Matched-terms method</p> <p>Under US GAAP, for hedges that do not qualify for the shortcut method, if the critical terms of the hedging instrument and the entire hedged item are the same, the entity can conclude that changes in fair value or cash flows attributable to the risk being hedged are expected to completely offset. An entity is not allowed to assume (1) no ineffectiveness when it exists or (2) that testing can be avoided. Rather, matched terms provide a simplified approach to effectiveness testing in certain situations.</p> <p>The SEC has clarified that the critical terms have to be perfectly matched to assume no ineffectiveness. Additionally, the critical-term-match method is not available for interest rate hedges.</p>	<p>Shortcut method</p> <p>IFRS does not allow a shortcut method by which an entity may assume no ineffectiveness.</p> <p>IFRS permits portions of risk to be designated as the hedged risk for financial instruments in a hedging relationship such as selected contractual cash flows or a portion of the fair value of the hedged item, which can improve the effectiveness of a hedging relationship. Nevertheless, entities are still required to test effectiveness and measure the amount of any ineffectiveness.</p> <p>Matched-terms method</p> <p>IFRS does not specifically discuss the methodology of applying a matched-terms approach in the level of detail included within US GAAP. However, if an entity can prove for hedges in which the principal terms of the hedging instrument and the hedged items are the same that the relationship will always be 100 percent effective based on an appropriately designed test, a similar qualitative analysis may be sufficient for prospective testing.</p> <p>Even if the principal terms are the same, retrospective effectiveness must be assessed and ineffectiveness must be measured in all cases because IFRS precludes the assumption of perfect effectiveness.</p>

Impact	US GAAP	IFRS
<p>Credit risk and hypothetical derivatives</p> <p>In a cash flow hedge, an entity's assessment of hedge effectiveness may be impacted by an entity's own credit risk or by the credit risk of the hedging derivative's counterparty. When using the hypothetical derivative method, a difference between IFRS and US GAAP may arise depending on: a) whether the derivative is in an asset or liability position and b) the method used for valuing liabilities.</p>	<p>Under US GAAP, a hypothetical derivative will reflect an adjustment for counterparty (or an entity's own) credit risk. This adjustment will be based upon the credit risk in the actual derivative. As such, no ineffectiveness will arise due to credit risk as the same risk is reflected in both the actual and hypothetical derivative.</p> <p>If, however, the likelihood that the counterparty will perform ceases to be probable, an entity would be unable to conclude that the hedging relationship in a cash flow hedge is expected to be highly effective in achieving offsetting cash flows. In those instances, the hedging relationship is discontinued.</p>	<p>Under IFRS, a hypothetical derivative perfectly matches the hedged risk of the hedged item. Since the hedged item would not contain the derivative counterparty's (or an entity's own) credit risk, the hypothetical derivative would not reflect that credit risk. The actual derivative, however, would reflect credit risk. The resulting mismatch between changes in the fair value of the hypothetical derivative and the hedging instrument would result in ineffectiveness.</p> <p>The extent of ineffectiveness depends on whether the hedging derivative instrument is in an asset or liability position and the method used for measuring derivative liabilities. This is because counterparty credit risk always affects the valuation of a derivative asset. If the derivative instrument is in a liability position, the ineffectiveness will depend on the method used to measure the liability.</p>

Impact	US GAAP	IFRS
Servicing rights Differences exist in the recognition and measurement of servicing rights, which may result in differences with respect to the hedging of servicing rights. This is especially relevant for the financial institutions that originate mortgages and retain the right to service them.	<p>US GAAP specifically permits servicing rights to be hedged for the benchmark interest rate or for overall changes in fair value in a fair value hedge.</p> <p>An entity may, however, avoid the need to apply hedge accounting by electing to measure servicing rights at fair value through profit or loss as both the hedging instrument and the hedged item would be measured at fair value through profit or loss.</p>	<p>Under IFRS, servicing rights are considered nonfinancial items. Accordingly, they can only be hedged for foreign currency risk or hedged in their entirety for all risks (i.e., not only for interest rate risk).</p> <p>Furthermore, IFRS precludes measurement of servicing rights at fair value through profit or loss because the fair value option is applicable only to financial items and therefore cannot be applied to servicing rights.</p>
Cash flow hedges with purchased options For cash flow hedges, US GAAP provides more flexibility than IFRS with respect to designating a purchased option as a hedging instrument. As a result of the difference, there may be more income statement volatility for IFRS entities using purchased options in their hedging strategies.	<p>US GAAP permits an entity to assess effectiveness based on total changes in the purchased option's cash flows (that is, the assessment will include the hedging instrument's entire change in fair value). As a result, the entire change in the option's fair value (including time value) may be deferred in equity based on the level of effectiveness.</p> <p>Alternatively, the hedge relationship can exclude time value from the hedging instrument such that effectiveness is assessed based on intrinsic value.</p>	<p>Under IFRS, when hedging one-sided risk via a purchased option in a cash flow hedge of a forecasted transaction, only the intrinsic value of the option is deemed to be reflective of the one-sided risk of the hedged item. Therefore, in order to achieve hedge accounting with purchased options, an entity will be required to separate the intrinsic value and time value of the purchased option and designate as the hedging instrument only the changes in the intrinsic value of the option.</p> <p>As a result, for hedge relationships where the critical terms of the purchased option match the hedged risk, generally, the change in intrinsic value will be deferred in equity while the change in time value will be recorded in the income statement.</p>

Impact	US GAAP	IFRS
<p>Foreign currency risk and internal derivatives</p> <p>Treasury centers that utilize internal derivatives and hedge net positions externally (as is common under US GAAP) will need to amend their approach and carefully assess the components of their net position if hedge accounting is to be retained and differences minimized.</p> <p>Restrictions under the IFRS guidance require that entities with treasury centers that desire hedge accounting either change their designation or enter into separate third-party hedging instruments for the gross amount of foreign currency exposures.</p>	<p>US GAAP permits hedge accounting for foreign currency risk with internal derivatives, provided specified criteria are met and, thus, accommodates the hedging of foreign currency risk on a net basis by a treasury center. The treasury center enters into derivatives contracts with unrelated third parties that would offset, on a net basis for each foreign currency, the foreign exchange risk arising from multiple internal derivative contracts.</p>	<p>Under IFRS, internal derivatives do not qualify for hedge accounting in the consolidated financial statements (because they are eliminated in consolidation). However, a treasury center's net position that is laid off to an external party may be designated as a hedge of a gross position in the consolidated financial statements. Careful consideration of the positions to be designated as hedged items may be necessary so as to minimize the effect of this difference. Entities may use internal derivatives as an audit trail or a tracking mechanism to relate external derivatives to the hedged item.</p> <p>The internal derivatives would qualify as hedging instruments in the separate financial statements of the subsidiaries entering into internal derivatives with a group treasury center.</p>

Impact	US GAAP	IFRS
Hedge accounting practices not allowed under US GAAP that are acceptable under IFRS		
<p>Hedges of a portion of the time period to maturity</p> <p>IFRS is more permissive than US GAAP with respect to a partial-term fair value hedge.</p>	<p>US GAAP does not permit the hedged risk to be defined as a portion of the time period to maturity of a hedged item.</p>	<p>IFRS permits designation of a derivative as hedging only a portion of the time period to maturity of a hedged item if effectiveness can be measured and the other hedge accounting criteria are met. For example, an entity with a 10 percent fixed bond with remaining maturity of 10 years can acquire a five-year pay-fixed, receive-floating swap and designate the swap as hedging the fair value exposure of the interest rate payments on the bond until the fifth year and the change in value of the principal payment due at maturity to the extent affected by changes in the yield curve relating to the five years of the swap. That is, a five-year bond is the imputed hedged item in the actual 10-year bond; the interest rate risk hedged is the five-year interest rate implicit in the 10-year bond.</p>

Impact	US GAAP	IFRS
<p>Designated risks for financial assets or liabilities</p> <p>IFRS provides opportunities with respect to achieving hedge accounting for a portion of a specified risk. Those opportunities may reduce the amount of ineffectiveness that needs to be recorded in the income statement under IFRS (when compared with US GAAP).</p>	<p>The guidance does not allow a portion of a specific risk to qualify as a hedged risk in a hedge of financial assets or financial liabilities. US GAAP specifies that the designated risk be in the form of changes in one of the following:</p> <ul style="list-style-type: none"> • Overall fair value or cash flows • Benchmark interest rates • Foreign currency exchange rates • Creditworthiness and credit risk <p>The interest rate risk that can be hedged is explicitly limited to specified benchmark interest rates.</p>	<p>The guidance allows a portion of a specific risk to qualify as a hedged risk (so long as effectiveness can be reliably measured). Designating a portion of a specific risk may reduce the amount of ineffectiveness that needs to be recorded in the income statement under IFRS compared to US GAAP.</p> <p>Under IFRS, portions of risks can be viewed as portions of the cash flows (e.g., excluding the credit spread from a fixed-rate bond in a fair value hedge of interest rate risk) or different types of financial risks, provided the types of risk are separately identifiable and effectiveness can be measured reliably.</p>
<p>Fair value hedge of interest rate risk in a portfolio of dissimilar items</p> <p>IFRS is more flexible than US GAAP with respect to the ability to achieve fair value hedge accounting in relation to interest rate risk within a portfolio of dissimilar items. That difference is especially relevant for financial institutions that use such hedging as a part of managing overall exposure to interest rate risk and may result in risk management strategies' being reflected as hedges under IFRS that do not qualify for hedge accounting under US GAAP.</p>	<p>US GAAP does not allow a fair value hedge of interest rate risk in a portfolio of dissimilar items.</p>	<p>IFRS allows a fair value hedge of interest rate risk in a portfolio of dissimilar items whereby the hedged portion may be designated as an amount of a currency, rather than as individual assets (or liabilities). Furthermore, an entity is able to incorporate changes in prepayment risk by using a simplified method set out in the guidance, rather than specifically calculating the fair value of the prepayment option on a (prepayable) item by item basis.</p> <p>In such a strategy, the change in fair value of the hedged item is presented in a separate line in the balance sheet and does not have to be allocated to individual assets or liabilities.</p>

Impact	US GAAP	IFRS
<p>Firm commitment to acquire a business</p> <p>IFRS permits entities to hedge, with respect to foreign exchange risk, a firm commitment to acquire a business in a business combination, which is precluded under US GAAP.</p>	<p>US GAAP specifically prohibits a firm commitment to enter into a business combination or acquire or dispose of a subsidiary, minority interest or equity method investee from qualifying as a hedged item for hedge accounting purposes (even if it is with respect to foreign currency risk).</p>	<p>An entity is permitted to hedge foreign exchange risk to a firm commitment to acquire a business in a business combination only for foreign exchange risk.</p> <p>Companies accounting for these types of hedges as cash flow hedges under IFRS establish a policy for releasing the cumulative amount recorded in equity to profit or loss. Once the transaction occurs, such amounts are released into profit or loss at the earlier of (1) goodwill impairment or (2) disposal of the acquiree.</p>
<p>Foreign currency risk and location of hedging instruments</p> <p>In hedging forecasted transactions and net investments for foreign currency exposure, IFRS provides an opportunity for a parent to hedge the exposures of an indirect subsidiary regardless of the functional currency of intervening entities within the organizational structure.</p>	<p>Under the guidance, either the operating unit that has the foreign currency exposure is a party to the hedging instrument or another member of the consolidated group that has the same functional currency as that operating unit is a party to the hedging instrument. However, for another member of the consolidated group to enter into the hedging instrument, there may be no intervening subsidiary with a different functional currency.</p>	<p>For foreign currency hedges of forecasted transactions, IFRS does not require the entity with the hedging instrument to have the same functional currency as the entity with the hedged item. At the same time, IFRS does not require that the operating unit exposed to the risk being hedged within the consolidated accounts be a party to the hedging instrument.</p> <p>As such, IFRS allows a parent company with a functional currency different from that of a subsidiary to hedge the subsidiary's transactional foreign currency exposure.</p> <p>The same flexibility regarding location of the hedging instrument applies to net investment hedges.</p>

Impact	US GAAP	IFRS
<p>Hedging more than one risk</p> <p>IFRS provides greater flexibility with respect to utilizing a single hedging instrument to hedge more than one risk in two or more hedged items. That difference may allow entities to adopt new and sometimes more complex strategies to achieve hedge accounting while managing certain risks.</p>	<p>US GAAP does not allow a single hedging instrument to hedge more than one risk in two or more hedged items. US GAAP does not permit creation of a hypothetical component in a hedging relationship to demonstrate hedge effectiveness in the hedging of more than one risk with a single hedging instrument.</p> <p>US GAAP permits cash flow hedge accounting if a hedging instrument (e.g., a basis swap) is used to modify the interest receipts or payments associated with a recognized financial asset or liability from one variable rate to another variable rate (i.e., one leg of the swap should be the same as the payment on the financial liability and the other leg of the swap should match the receipt on the financial asset).</p>	<p>IFRS permits designation of a single hedging instrument to hedge more than one risk in two or more hedged items. A single hedging instrument may be designated as a hedge of more than one type of risk if the risks hedged can be identified clearly, the effectiveness of the hedge can be demonstrated and it is possible to ensure that there is specific designation of the hedging instrument and different risk positions. In the application of this guidance, a single swap may be separated by inserting an additional (hypothetical) leg, provided that each portion of the contract is designated as a hedging instrument in a qualifying and effective hedge relationship.</p>

Impact	US GAAP	IFRS
<p>Cash flow hedges and basis adjustments on acquisition of nonfinancial items</p> <p>In the context of a cash flow hedge, IFRS permits more flexibility regarding the presentation of amounts that have accumulated in equity (resulting from a cash flow hedge of nonfinancial assets and liabilities).</p> <p>Therefore, the balance sheet impacts may be different depending on the policy election made by entities for IFRS purposes. The income statement impact, however, is the same regardless of this policy election.</p>	<p>In the context of a cash flow hedge, US GAAP does not permit basis adjustments. That is, under US GAAP, an entity is not permitted to adjust the initial carrying amount of the hedged item by the cumulative amount of the hedging instruments' fair value changes that were recorded in equity.</p> <p>US GAAP does refer to "basis adjustments" in a different context wherein the term is used to refer to the method by which, in a fair value hedge, the hedged item is adjusted for changes in its fair value attributable to the hedged risk.</p>	<p>Under IFRS, <i>basis adjustment</i> commonly refers to an adjustment of the initial carrying value of a nonfinancial asset or nonfinancial liability that resulted from a forecasted transaction subject to a cash flow hedge. That is, the initial carrying amount of the nonfinancial item recognized on the balance sheet (i.e., the basis of the hedged item) is adjusted by the cumulative amount of the hedging instrument's fair value changes that were recorded in equity.</p> <p>IFRS gives entities an accounting policy choice to either basis adjust the hedged item (if it is a nonfinancial item) or release amounts to profit or loss as the hedged item affects earnings.</p>

Technical references

IFRS IAS 39, IFRS 7, IFRIC 9, IFRIC 16

US GAAP ASC 815, ASC 815-20-25-3, ASC 815-15-25-4 through 25-5, ASC 815-20-25-94 through 25-97, ASC 830-30-40-2 through 40-4

Note

The foregoing discussion captures a number of the more significant GAAP differences. It is important to note that the discussion is not inclusive of all GAAP differences in this area.

Recent/proposed guidance

FASB Exposure Draft on Accounting for Hedging Activities

On June 6, 2008, the FASB issued an exposure draft to amend the accounting for hedging activities and other related literature. The comment period ended on August 15, 2008. The objective of the proposed Standard is to simplify the accounting for hedging activities, resolve hedge accounting practice issues that have arisen under the current guidance and make the hedge accounting model and associated disclosures more useful and understandable to financial statement users.

The exposure draft would eliminate:

- The shortcut method and critical-terms match method
- The right to designate individual risks as hedged risk, except in the case of foreign currency risk and hedges of interest rate risk on a company's own debt at inception of the debt
- The requirement to quantitatively assess hedge effectiveness on an ongoing basis in order to qualify for hedge accounting

In addition, the exposure draft would enable companies to qualify for hedge accounting by performing a qualitative assessment at inception of the hedging relationship demonstrating that:

- An economic relationship exists between the hedging instrument and the hedged transaction
- The derivative would be expected to reasonably offset the change in fair value of the hedged item

After inception, companies would need to reassess hedge effectiveness only if circumstances suggest that the hedging relationship may no longer be reasonably effective.

Redeliberations on the hedging project have been delayed pending a decision on the financial instruments research project. As hedging is a subset of that project, the Board decided to wait for the agenda decision to be made before continuing work on the hedging project.

This project has the potential to create significant differences when compared with current IFRS. However, both the IASB and FASB are coordinating efforts in a project to produce new guidance for hedge accounting.

Financial instruments: replacement of IAS 39

In March 2008 the IASB released a discussion paper that discusses the main causes of complexity in reporting financial instruments. It also discusses possible intermediate and long-term approaches to improving financial reporting and reducing complexity. The IASB has noted that many preparers of financial statements, their auditors and users of financial statements find the requirements for reporting financial instruments complex. The IASB and the FASB have been urged by many to develop new standards of financial reporting for financial instruments that are principles-based and less complex than today's requirements. As a result of the financial crisis, work on this project was accelerated to change the accounting for financial instruments. The replacement of IAS 39 project is being broken down into three stages, (1) classification and measurement of financial assets and liabilities, (2) impairment and (3) hedge accounting. The IASB is expected to release exposure drafts over the remainder of

2009 with classification and measurement already released in July 2009, impairment in October 2009 and hedge accounting in December 2009, with final standards in time for year-end financial statements for 2009 (classification and measurement) and during 2010 (impairment and hedge accounting). The classification and measurement project is expected to eliminate the requirement to evaluate embedded derivatives in financial instruments.

This project has the potential to create significant differences when compared with current US GAAP. However, both the IASB and FASB are coordinating efforts in their projects to reduce complexity in reporting financial instruments, although the ultimate standards may not be fully converged.

FASB Implementation Issue on *Exceptions Related to Embedded Credit Derivatives*

The objective of this project is to resolve some potential ambiguity about the embedded credit derivatives scope exception in ASC 815 by providing clarifying language regarding when embedded credit derivative features, including those in CDOs and synthetic CDOs, are not considered embedded derivatives subject to potential bifurcation and separate accounting.

On June 3, 2009, the Board decided to re-expose a revised proposed Implementation Issue for a 45-day comment period. The effective date of the revised proposed Implementation Issue will be the first day of each reporting entity's first fiscal quarter beginning after December 15, 2009. The revised Implementation Issue is expected to close the current difference between IFRS and US GAAP related to synthetic CDOs.

Consolidation

Consolidation

IFRS is a principles-based framework, and the approach to consolidation reflects that structure. IFRS provides indicators of control, some of which individually determine the need to consolidate. However, where control is not apparent, consolidation is based on an overall assessment of all of the relevant facts, including the allocation of risks and benefits between the parties. The indicators provided under IFRS help the reporting entity in making that assessment. Consolidation is required under IFRS when an entity has the ability to govern the financial and operating policies of another entity to obtain benefits.

US GAAP has a two-tiered consolidation model: one focused on the voting rights (the voting interest model) and the second based on a party's exposure to the risks and rewards of an entity's activities (the variable interest model). Under US GAAP, all entities are evaluated to determine whether they are variable-interest entities (VIEs). Consolidation of all non-VIEs is assessed on the basis of voting and other decision-making rights. Even in cases where both US GAAP and IFRS look to voting rights to drive consolidation, differences can arise. Examples include cases where de facto control exists, how the two bodies of GAAP address potential voting rights, and finance structures such as investment funds. As a result, careful analysis is required to identify any differences. The FASB recently issued guidance on the consolidation of VIEs that will be effective January 1, 2010, for calendar year-end companies. The new guidance requires an entity with a variable interest in a VIE to qualitatively assess whether it has a financial interest in the entity and, if so, whether it is the primary beneficiary. This significantly changes previous guidance, moving to a qualitative analysis from a quantitative analysis.

With the issuance of guidance on noncontrolling interests in consolidated financial statements, there were significant changes within US GAAP effective for fiscal years beginning on or after December 15, 2008. Significant changes introduced by the new guidance include:

- Noncontrolling interest (previously referred to as minority interest) is reported as part of equity in the consolidated financial statements.
- Losses are allocated to the noncontrolling interest even when such allocation might result in a deficit balance. This reduces the losses attributed to the controlling interest.
- In cases where control is maintained, changes in ownership interests are treated as equity transactions. Differences between the fair value of the consideration received or paid and the related carrying value of the noncontrolling interest are recognized in the controlling interest's equity.
- Upon a loss of control, any gain or loss on the interest sold is recognized in earnings. Additionally, any ownership or contractual interest retained is remeasured at fair value on the date control is lost, with any gain or loss being recognized in earnings.

The new guidance also changes the accounting and reporting for the deconsolidation of a subsidiary. Most organizations will be impacted by the major changes in accounting for noncontrolling interests and the accounting for the deconsolidation of a subsidiary.

IAS 27 (Revised), *Consolidated and Separate Financial Statements*, must be applied for annual periods beginning on or after July 1, 2009. Earlier application is permitted. However, an entity must not apply the amendments for annual periods beginning before July 1, 2009, unless it also applies IFRS 3, *Business Combinations* (as revised in 2008). IAS 27 (Revised) does not change the presentation of noncontrolling interests from the previous standard, which is similar to the new requirements under US GAAP; however, additional disclosures are required to show the effect of transactions with noncontrolling interests on the equity attributable to parent company shareholders. IAS 27 (Revised) and the recently issued guidance under US GAAP have converged in the broad principles, particularly related to the reporting of noncontrolling interests in subsidiaries. However, the standards have not been developed using consistent language.

For jointly controlled entities, IFRS provides an option for proportional consolidation; the proportional method is allowed only under US GAAP for unincorporated entities in certain industries.

Differences in consolidation under US GAAP and IFRS may also arise in the event a subsidiary's set of accounting policies differs from that of the parent. While under US GAAP it is acceptable to apply different accounting policies within a consolidation group to address issues relevant to certain specialized industries, exceptions to the requirement to consistently apply standards in a consolidated group are very limited under IFRS. In addition, potential adjustments may occur in situations where a parent company has a fiscal year-end different from that of a consolidated subsidiary (and the subsidiary is consolidated on a lag). Under US GAAP, significant transactions in the gap period may require disclosure only, while IFRS may require that transactions in the gap period be recognized in the consolidated financial statements.

Further details on the foregoing and other selected differences are described in the following table.

Impact	US GAAP	IFRS
General requirements		
<p>Requirements to prepare consolidated financial statements</p> <p>IFRS does not provide industry-specific exceptions (e.g., investment companies and broker/dealers) to the requirement for consolidation of controlled entities. However, IFRS is, in limited circumstances, more flexible with respect to the right to issue nonconsolidated financial statements.</p>	<p>The guidance applies to legal structures. Industry-specific guidance precludes consolidation of controlled entities by certain types of organizations, such as registered investment companies or broker/dealers.</p> <p>Consolidated financial statements are presumed to be more meaningful and are required for SEC registrants.</p> <p>There are no exemptions for consolidating subsidiaries in general-purpose financial statements.</p>	<p>Parent entities prepare consolidated financial statements that include all subsidiaries. An exemption applies to a parent entity when all of the following conditions apply:</p> <ul style="list-style-type: none"> • That is itself wholly owned or if the owners of the minority interests have been informed about and do not object to the parent's not presenting consolidated financial statements • When the parent's debt or equity securities are not publicly traded and the parent is not in the process of issuing securities in public securities markets • When the immediate or ultimate parent publishes consolidated financial statements that comply with IFRS <p>A subsidiary is not excluded from consolidation simply because the investor is a venture capital organization, mutual fund, unit trust or similar entity.</p> <p>The guidance applies to activities regardless of whether they are conducted by a legal entity.</p>

Impact	US GAAP	IFRS
<p>Consolidation model</p> <p>Differences in consolidation can arise due to:</p> <ul style="list-style-type: none"> • Differences in how economic benefits are evaluated when the consolidation assessment considers more than just voting rights (i.e., differences in methodology) • Specific differences or exceptions such as: <ul style="list-style-type: none"> - The consideration of variable interests - Concepts of de facto control - How potential voting rights are evaluated - Guidance related to de facto agents, etc. - Reconsideration events 	<p>All consolidation decisions are evaluated first under the VIE model.</p> <p>US GAAP requires an entity with a variable interest in a VIE to qualitatively assess the determination of the primary beneficiary of a VIE.</p> <p>In applying the qualitative model an entity is deemed to have a controlling financial interest if it meets both of the following criteria:</p> <ul style="list-style-type: none"> • Power to direct activities of the VIE that most significantly impact the VIE's economic performance ("power criterion") • Obligation to absorb losses from or right to receive benefits of the VIE that could potentially be significant to the VIE ("losses/benefits criterion") <p>In assessing whether an enterprise has a controlling financial interest in an entity, it should consider the entity's purpose and design, including the risks that the entity was designed to create and pass through to its variable interest holders.</p> <p>Only one enterprise, if any, is expected to be identified as the primary beneficiary of a VIE. Although more than one enterprise could meet the losses/benefits criterion, only one enterprise, if any, will have the power to direct the activities of a VIE that most significantly impacts the entity's economic performance.</p>	<p>IFRS focuses on the concept of control in determining whether a parent-subsidiary relationship exists. Control is the parent's ability to govern the financial and operating policies of a subsidiary to obtain benefits. Control is presumed to exist when a parent owns, directly or indirectly, more than 50 percent of an entity's voting power.</p> <p>IFRS specifically requires potential voting rights to be assessed. Instruments that are currently exercisable or convertible are included in the assessment, with no requirement to assess whether exercise is economically reasonable (provided such rights have economic substance).</p> <p>Control also exists when a parent owns half or less of the voting power, but has legal or contractual rights to control the majority of the entity's voting power or board of directors.</p> <p>In rare circumstances, a parent could also have control over an entity in circumstances where it holds less than 50 percent of the voting rights of an entity and lacks legal or contractual rights by which to control the majority of the entity's voting power or board of directors (de facto control). An example of de facto control is when a major shareholder holds an investment in an entity with an otherwise dispersed public shareholding. The assertion of de facto control is evaluated on the basis of all relevant facts and circumstances, including the legal and regulatory environment, the nature of the capital market and the ability of the majority owners of voting shares to vote together.</p>

Impact	US GAAP	IFRS
Consolidation model (continued)	<p>Increased skepticism should be given to situations in which an enterprise's economic interest in a VIE is disproportionately greater than its stated power to direct the activities of a VIE that most significantly impact the entity's economic performance. As the level of disparity increases, the level of skepticism about an enterprise's lack of power is expected to increase.</p> <p>US GAAP also includes specific guidance on interests held by related parties. A related-party group includes the reporting entity's related parties and de facto agents (e.g., close business advisers, partners, employees, etc.) whose actions are likely to be influenced or controlled by the reporting entity.</p> <p>Individual parties within a related party group (including de facto agency relationships) are required to first separately consider whether they meet both the power and losses/benefits criteria. If one party within the related party group meets both criteria, it is the primary beneficiary of the VIE. If no party within the related party group on its own meets both criteria, the determination of the primary beneficiary within the related party group is based on an analysis of the facts and circumstances with the objective of determining which party is most closely associated with the VIE.</p>	<p>IFRS does not address the impact of related parties and de facto agents. There is no concept of a trigger event under IFRS.</p> <p>Control may exist even in cases where an entity owns little or none of a special-purpose entities (SPEs) equity. The application of the control concept requires, in each case, judgment in the context of all relevant factors.</p> <p>IFRS does not provide explicit guidance on silos. However, it does create an obligation to consider whether a corporation, trust, partnership or other unincorporated entity has been created to accomplish a narrow and well-defined objective. The governing document of such entities may impose strict and sometimes permanent limits on the decision-making ability of the board, trustees, etc. IFRS requires the consideration of substance over form and discrete activities within a much larger operating entity to fall within its scope. When an SPE is identified within a larger entity (including a non-SPE), the SPE's economic risks, rewards and design are assessed in the same manner as any legal entity's.</p>

Impact	US GAAP	IFRS
Consolidation model (continued)	<p>Determination of whether an entity is a VIE gets reconsidered either when a specific reconsideration event occurs or, in the case of a voting interest entity, when voting interests or rights change.</p> <p>However, the determination of a VIE's primary beneficiary is an ongoing assessment.</p> <p>While US GAAP applies to legal structures, the FASB has included guidance to address circumstances in which an entity with a variable interest shall treat a portion of the entity as a separate VIE if specific assets or activities (a silo) are essentially the only source of payment for specified liabilities or specified other interests. A party that holds a variable interest in the silo then assesses whether it is the silo's primary beneficiary. The key distinction is that the US GAAP silo guidance applies only when the larger entity is a VIE.</p> <p>All other entities are evaluated under the voting interest model. Unlike IFRS, only actual voting rights are considered. Under the voting interest model, control can be direct or indirect. In certain unusual circumstances, control may exist with less than 50 percent ownership, when contractually supported. The concept is referred to as effective control.</p>	<p>When control of an SPE is not apparent, IFRS requires evaluation of every entity—based on the entity's characteristics as a whole—to determine the controlling party. The concept of economic benefit or risk is just one part of the analysis. Other factors considered in the evaluation are the entity's design (e.g., auto-pilot), the nature of the entity's activities and the entity's governance.</p> <p>The substance of the arrangement would be considered in order to decide the controlling party for IFRS purposes.</p>

Impact	US GAAP	IFRS
<p>Special-purpose entities</p> <p>Differences in consolidation can arise due to differences in the definition of VIE versus SPE, including scope exceptions (i.e., scope differences).</p>	<p>Consolidation requirements focus on whether an entity is a VIE regardless of whether it would be considered an SPE.</p> <p>Often, an SPE would be considered a VIE because since they are typically narrow in scope, often highly structured and thinly capitalized, but this is not always the case. For example, clear SPEs benefit from exceptions to the variable interest model such as pension, postretirement or postemployment plans.</p> <p>The guidance above applies only to legal entities.</p>	<p>Decision-making rights are not always indicative of control, particularly in the case of an SPE where decision-making rights may be either severely limited (on autopilot) or structured for a narrow, well-defined purpose (such as a lease or securitization). As a result, IFRS requires other indicators of control to be considered. Those indicators are as follows:</p> <ul style="list-style-type: none"> • Whether the SPE conducts its activities on behalf of the evaluating entity • Whether the evaluating entity has the decision-making power to obtain the majority of the benefits of the SPE • Whether the evaluating entity has the right to obtain the majority of the benefits of the SPE • Whether the evaluating entity has the majority of the residual or ownership risks of the SPE or its assets <p>This guidance is applied to all SPEs with the exception of postemployment benefit plans or other long-term employee benefit plans.</p> <p>The guidance above applies to activities regardless of whether they are conducted by a legal entity.</p>

Impact	US GAAP	IFRS
<p>Accounting policies and reporting periods</p> <p>In relation to certain specialized industries, US GAAP allows more flexibility for utilization of different accounting policies within a single set of consolidated financial statements.</p> <p>In the event of nonuniform reporting periods, the treatment of significant transactions in any gap period varies under the two frameworks, with the potential for earlier recognition under IFRS.</p>	<p>Consolidated financial statements are prepared by using uniform accounting policies for all of the entities in a group. Limited exceptions exist when a subsidiary has specialized industry accounting principles. Retention of the specialized accounting policy in consolidation is permitted in such cases.</p> <p>The consolidated financial statements of the parent and the subsidiary are usually drawn up at the same reporting date. However, the consolidation of subsidiary accounts can be drawn up at a different reporting date, provided the difference between the reporting dates is no more than three months. Adjustments are generally not made for transactions that occur in the gap period. Disclosure of significant events is required.</p>	<p>Consolidated financial statements are prepared by using uniform accounting policies for like transactions and events in similar circumstances for all of the entities in a group.</p> <p>The consolidated financial statements of the parent and the subsidiary are usually drawn up at the same reporting date. However, the subsidiary accounts as of a different reporting date can be consolidated, provided the difference between the reporting dates is no more than three months. Unlike US GAAP, adjustments are made to the financial statements for significant transactions that occur in the gap period.</p>

Impact	US GAAP	IFRS
Disclosures US GAAP requires greater disclosure about an entity's involvement in VIEs/SPEs	<p>Applies to both nonpublic and public enterprises.</p> <p>The principal objectives of disclosures are to provide financial statement users with an understanding of the following:</p> <ul style="list-style-type: none"> • Significant judgments and assumptions made by an enterprise in determining whether it must consolidate a VIE and/or disclose information about its involvement in a VIE • The nature of restrictions on a consolidated VIE's assets and on the settlement of its liabilities reported by an enterprise in its statement of financial position, including the carrying amounts of such assets and liabilities • The nature of, and changes in, the risks associated with an enterprise's involvement with the VIE • How an enterprise's involvement with the VIE affects the enterprise's financial position, financial performance, and cash flows <p>The level of disclosure to achieve these objectives may depend on the facts and circumstances surrounding the VIE and the enterprise's interest in that entity.</p> <p>US GAAP provides additional detailed disclosure guidance in order to meet the objectives described above.</p>	<p>IFRS does not have SPE-specific disclosure requirements.</p> <p>IFRS has several consolidation disclosure requirements, which include the following:</p> <ul style="list-style-type: none"> • Nature of relationship between parent and a subsidiary when parent does not own, directly or indirectly through subsidiaries, more than half of voting power • Reasons why ownership, directly or indirectly through subsidiaries, of more than half of voting or potential voting power of an investee does not constitute control • Date of financial statements of a subsidiary when such financial statements are used to prepare consolidated financial statements and are as of a date or for a period that is different from that of the parent's financial statements, and the reason for using a different date or period • Nature and extent of any significant restrictions (e.g., resulting from borrowing arrangements or regulatory requirements) on ability of subsidiaries to transfer funds to parent in the form of cash dividends or to repay loans or advances

Impact	US GAAP	IFRS
Disclosures (continued)	<p>Guidance also calls for certain specific disclosures to be made by (1) a primary beneficiary of a VIE, and (2) an enterprise that holds a variable interest in a VIE (but is not the primary beneficiary).</p>	<ul style="list-style-type: none"> • Schedule that shows effects of changes in a parent's ownership interest in a subsidiary that do not result in a loss of control on equity attributable to owners of parent • If control of a subsidiary is lost, the parent shall disclose the gain or loss, if any, and: <ol style="list-style-type: none"> 1. Portion of that gain or loss attributable to recognizing any investment retained in former subsidiary at its fair value at date when control is lost 2. Line item(s) in the statement of comprehensive income in which gain or loss is recognized (if not presented separately in the statement of comprehensive income) <p>Additional disclosures are required in instances when separate financial statements are prepared for a parent that elects not to prepare consolidated financial statements, or when a parent, venturer with an interest in a jointly controlled entity or an investor in an associate prepares separate financial statements.</p>

Impact	US GAAP	IFRS
Equity investments/investments in associates		
Conforming accounting policies Under IFRS, entities must conform policies for all associates, which may affect reported figures (assets, liabilities and earnings), covenants and ratios.	The equity investee's accounting policies do not have to conform to the investor's accounting policies if the investee follows an acceptable alternative US GAAP treatment.	An investor's financial statements are prepared by using uniform accounting policies for similar transactions and events.
Definition and types Differences in the definition or types of joint ventures may result in different arrangements being considered joint ventures, which could affect reported figures, earnings, ratios and covenants.	<p>The term joint venture refers only to jointly controlled entities, where the arrangement is carried on through a separate entity.</p> <p>A corporate joint venture is defined as a corporation owned and operated by a small group of businesses as a separate and specific business or project for the mutual benefit of the members of the group.</p> <p>Most joint venture arrangements give each venturer (investor) participating rights over the joint venture (with no single venturer having unilateral control), and each party sharing control must consent to the venture's operating, investing and financing decisions.</p>	<p>A joint venture is defined as a contractual agreement whereby two or more parties undertake an economic activity that is subject to joint control. Joint control is the contractually agreed sharing of control of an economic activity. Unanimous consent of the parties sharing control, but not necessarily all parties in the venture, is required.</p> <p>IFRS distinguishes between three types of joint ventures:</p> <ul style="list-style-type: none"> • Jointly controlled entities, in which the arrangement is carried on through a separate entity (company or partnership) • Jointly controlled operations, in which each venturer uses its own assets for a specific project • Jointly controlled assets, which is a project carried on with assets that are jointly owned

Impact	US GAAP	IFRS
<p>Accounting for joint venture arrangements</p> <p>IFRS provides an option for proportional consolidation of jointly controlled entities. Under US GAAP, the proportional method is allowed only for entities in certain industries. Refer to the Recent/Proposed Guidance section for potential changes in this area.</p>	<p>Prior to determining the accounting model, an entity first assesses whether the joint venture is a VIE. If the joint venture is a VIE, the accounting model discussed earlier is applied. Joint ventures often have a variety of service, purchase and/or sales agreements as well as funding and other arrangements that may affect the entity's status as a VIE. Equity interests are often split 50-50 or near 50-50, making nonequity interests (i.e., any variable interests) highly relevant in consolidation decisions. Careful consideration of all relevant contracts and governing documents is critical in the determination of whether a joint venture is within the scope of the variable interest model and, if so, whether consolidation is required.</p> <p>If the joint venture is not a VIE, venturers apply the equity method to recognize the investment in a jointly controlled entity. Proportionate consolidation is generally not permitted except for unincorporated entities operating in certain industries. A full understanding of the rights and responsibilities conveyed in management, shareholder and other governing documents is necessary.</p>	<p>Either the proportionate consolidation method or the equity method is allowed to account for a jointly controlled entity (a policy decision that must be applied consistently). Proportionate consolidation requires the venturer's share of the assets, liabilities, income and expenses to be either combined on a line-by-line basis with similar items in the venturer's financial statements or reported as separate line items in the venturer's financial statements. A full understanding of the rights and responsibilities conveyed in management agreements is necessary.</p>

Impact	US GAAP	IFRS
<p>Accounting for contributions to a jointly controlled entity</p> <p>Gain recognition upon contribution to a jointly controlled entity is more likely under IFRS.</p>	<p>As a general rule, a venturer records its contributions to a joint venture at cost (i.e., the amount of cash contributed and the carrying value of other nonmonetary assets contributed).</p> <p>When a venturer contributes appreciated noncash assets and others have invested cash or other hard assets, it may be appropriate to recognize a gain for a portion of that appreciation. Practice and existing literature vary in this area. As a result, the specific facts and circumstances affect gain recognition and require careful analysis.</p>	<p>A venturer that contributes nonmonetary assets, such as shares, property plant and equipment or intangible assets, to a jointly controlled entity in exchange for an equity interest in the jointly controlled entity recognizes in its consolidated income statement the portion of the gain or loss attributable to the equity interests of the other venturers, except when:</p> <ul style="list-style-type: none"> • The significant risks and rewards of the contributed assets have not been transferred to the jointly controlled entity; • The gain or loss on the assets contributed cannot be measured reliably; or • The contribution transaction lacks commercial substance.

Technical references

IFRS IAS 1, IAS 27, IAS 27(Revised), IAS 28, IAS 36, IAS 39, IFRS 5, SIC 12, SIC 13

US GAAP ASC 205, ASC 323, ASC 323-10-15-8 through 15-11, ASC 325-20, ASC 360, ASC 810, ASC 810-10-25-1 through 25-14, ASC 810-10-60-4, SAB Topic 5H, SAB Topic 5-H (2)-(6)

Note

The foregoing discussion captures a number of the more significant GAAP differences. It is important to note that the discussion is not inclusive of all GAAP differences in this area.

Recent/proposed guidance

Consolidation of Variable Interest Entities

The new guidance (discussed in the consolidation model above) amends the consolidation guidance for VIEs and comes in response to the perceived flaws in the accounting model, highlighted most recently by the economic downturn. It is intended to address concerns about the preparer's ability to structure transactions to avoid consolidation, balanced with the need for more relevant, timely, and reliable information about an enterprise's involvement in a VIE.

Key provisions of the new guidance include:

- The exemption for qualified special purpose entities from consolidation is eliminated. Consequently, these entities are subject to the provisions of the new guidance.
- A qualitative model, with the primary beneficiary being the variable interest holder that has (1) the power to direct the activities that most significantly impact the economic performance of the VIE, and (2) the obligation to absorb losses or the right to receive benefits of the VIE that could potentially be significant to the VIE. The related party tie-breaker is only applicable when there is no individual party within the related party group that is the primary beneficiary on a standalone basis.
- Substantive removal rights are not considered in determining whether as a group, the holders of the equity investment at risk lack power or the obligation to absorb expected losses or the right to expected residual returns unless one party has the unilateral ability to exercise those rights.
- A VIE's primary beneficiary is an ongoing assessment.
- Reconsideration of an entity's status as a VIE is still based on the occurrence of certain events. However, the troubled debt restructuring exception is removed and an additional reconsideration event has been added when the equity holders lose the power to direct activities of the entity that most significantly impact its economic performance. This will result in more entities becoming VIEs.
- The criteria for determining whether service provider or decision maker contracts are variable interests have changed. As a result, certain contracts will no longer be considered variable interests (and therefore will not be subject to the consolidation model).

While public enterprises were already required to provide significant new disclosures for VIEs under previously issued guidance for *Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities*, the new guidelines expand the scope of these disclosures to all enterprises and make some changes to what was previously required.

This guidance will be effective for calendar year-end companies as of January 1, 2010.

The issuance of this guidance does not converge US GAAP with IFRS. Therefore, differences will still exist between the two standards.

Exposure Draft 9, *Joint Arrangements*

In September 2007, the IASB issued Exposure Draft 9, *Joint Arrangements*, which would amend existing provisions of IAS 31. The exposure draft's core principle is that parties to a joint arrangement recognize their contractual rights and obligations arising from the arrangement. The exposure draft therefore focuses on the recognition of assets and liabilities by the parties to the joint arrangement. The scope of the exposure draft is broadly the same as that of IAS 31. That is, unanimous agreement is required between the key parties that have the power to make financial and operating policy decisions for the joint arrangement.

Exposure Draft 9 proposes two key changes. The first is the elimination of proportionate consolidation for a jointly controlled entity. This is expected to bring improved comparability between entities by removing the policy choice. The elimination of proportionate consolidation will have a fundamental impact on the income statement and balance sheet for some entities. Entities that currently use proportionate consolidation to account for jointly controlled entities may need to account for many of the latter by using the equity method. These entities will replace the line-by-line proportionate consolidation of the income statement and balance sheet by a single net result and a single net investment balance.

The second change is the introduction of a dual approach to the accounting for joint arrangements. Exposure Draft 9 originally carried forward—with modification from IAS 31—the three types of joint arrangement, each type having specific accounting requirements. The first two types are Joint Operations and Joint Assets. The description of these types and the accounting for them is consistent with Jointly Controlled Operations and Jointly Controlled Assets in IAS 31. In May 2009, the Board reached a tentative decision to merge Joint Operations and Joint Assets into a single type of joint arrangement called Joint Operations. The remaining type of joint arrangement is a Joint Venture, which is accounted for by using equity accounting. A Joint Venture is identified by the party having rights to only a share of the outcome of the joint arrangement—for example, a share of the profit or loss of the joint arrangement. The key change is that a single joint arrangement may contain more than one type—for example, Joint Assets and a Joint Venture. Parties to such a joint arrangement account first for the assets and liabilities of the Joint Assets arrangement and then use a residual approach to equity accounting for the Joint Venture part of the joint arrangement.

The Board continues its discussions. The final standard is expected to be issued in the second half of 2009. As drafted the exposure draft broadly achieves convergence in principle with US GAAP, which generally requires the use of the equity method to account for jointly controlled entities.

Exposure Draft, Consolidated Financial Statements

The International Accounting Standards Board initiated its project on consolidated financial statements with the objective of publishing a single IFRS on consolidation to replace the consolidation requirements in IAS 27, *Consolidated and Separate Financial Statements and SIC-12 Consolidation—Special Purpose Entities*. The main objectives of the project are to improve the definition of control and related application guidance so that a control model can be applied to all entities, and to improve the disclosure requirements about consolidated and unconsolidated entities. An exposure draft was issued in December 2008. The final standard is expected to be issued in the second half of 2009.

In addition to the proposals in this exposure draft, the Board is also reviewing, in a separate project, its requirements for the derecognition of financial instruments. The derecognition of financial instruments sometimes involves the use of structured entities. Therefore the projects on consolidation and derecognition of financial instruments are closely related in those circumstances. The Board would have preferred to publish exposure drafts for these projects at the same time. However, in response to the wide demand for a revised consolidation standard, the Board decided not to delay publication of the consolidation exposure draft. The Board published its exposure draft on the derecognition of financial instruments in March 2009.

The FASB recently issued guidance related to the consolidation of variable interest entities (see discussion above under “Consolidation of Variable Interest Entities,” and “Accounting for Transfers of Financial Assets” in the Financial Assets section under Recent/Proposed Guidance. Although the IASB and FASB have not conducted their work jointly, the boards have shared information as the related projects have progressed. Both Boards proposed introducing similar control-based consolidation requirements and disclosures for structured entities (variable interest entities). However, in contrast to the FASB’s issued guidance, the proposed IFRS would apply to all entities. The Boards plan to investigate ways to conduct their consolidation projects as a joint project in the future.

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Business combinations

Business combinations

IFRS and US GAAP have largely converged with IFRS in this area. Upon the release of the recently revised business combination standards, many historical differences have been eliminated, although certain important differences will remain. The new standards have eliminated historical differences related to a number of areas (e.g., the definition of a business, the accounting for restructuring provisions in a business combination, the determination of value for share-based consideration, accounting for in-process research and development and subsequent adjustments to assets acquired and liabilities assumed, to name a few). In addition, there were some significant changes to practice under both frameworks, for example, both new standards require companies to recognize transaction costs (e.g., professional fees) as period costs.

It is expected that the pervasive impact of the new guidance on accounting practices will have an immediate and lasting impact on the mergers and acquisitions environment. Finance leaders, deal makers and senior executives need to be aware of the impact the new standards will have on their business and future transactions. The accounting and disclosure requirements are likely to have considerable influence on the negotiation of and planning for merger transactions and communications with shareholders.

Under US GAAP, the revised business combinations guidance continues the movement toward (1) greater use of fair value in financial reporting and (2) transparency through expanded disclosures. It changes how business acquisitions are accounted for under US GAAP and will affect financial statements at the acquisition date and in subsequent periods.

IFRS 3 (Revised) is applied prospectively to business combinations occurring in the first annual period beginning on or after July 1, 2009. It can be applied early, but only to an annual period beginning on or after June 30, 2007. IFRS 3 (Revised) and IAS 27 (Revised) (see the Consolidation section for additional discussion on IAS 27 (Revised)) are to be applied at the same time. For IFRS, a filer's retrospective application to earlier business combinations is not permitted unless it is being applied in conjunction with a first-time adoption of IFRS. IFRS 3 (Revised) represents significant changes under IFRS, but is less of a radical change than the comparable standard in US GAAP.

The business combinations standards under US GAAP and IFRS are very close in principles and language, with two major exceptions: (1) full goodwill and (2) the requirements regarding recognition of contingent assets and contingent liabilities. Significant differences continue to exist in subsequent accounting. Different requirements for impairment testing and accounting for deferred taxes are among the most significant.

The following table identifies and discusses differences in the application of IFRS and US GAAP upon the adoption of the new standards.

Impact	US GAAP	IFRS	
Costs of acquisitions			
Contingent consideration	<p>The accounting for contingent consideration has moved to being recorded at fair value. In addition, differences between IFRS and US GAAP may create differences in the initial classification of contingent consideration and, therefore, might cause differences in the subsequent accounting.</p>	<p>Contingent consideration is recognized initially at fair value as either an asset, liability or equity according to the applicable US GAAP guidance.</p> <p>Contingent consideration classified as an asset or a liability is remeasured to fair value at each reporting date until the contingency is resolved. The changes in fair value are recognized in earnings unless the arrangement is a hedging instrument for which ASC 815, as amended by the new business combination guidance (included in ASC 805), requires the changes to be initially recognized in other comprehensive income.</p> <p>Contingent consideration classified as equity is not remeasured at each reporting date. Settlement is accounted for within equity.</p>	<p>Contingent consideration is recognized initially at fair value as either an asset, liability or equity according to the applicable IFRS guidance.</p> <p>Contingent consideration classified as an asset or a liability will likely be a financial instrument measured at fair value, with any gains or losses recognized in profit or loss (or OCI, as appropriate). Contingent consideration classified as an asset or liability that is not a financial instrument is subsequently accounted for in accordance with the provisions standard or other IFRSs as appropriate.</p> <p>Contingent consideration classified as equity is not remeasured. Settlement is accounted for within equity.</p>
Acquired assets and liabilities			
Acquired contingencies	<p>There are significant differences related to the recognition, and potentially measurement, of noncontractual contingencies, as well as the recognition of contingent assets.</p>	<p>Acquired liabilities and assets subject to contractual contingencies are recognized at fair value if fair value can be determined during the measurement period. If fair value cannot be determined, companies should typically account for the acquired contingencies using existing guidance. An acquirer shall develop a systematic and rational basis for subsequently measuring and accounting for assets and liabilities arising from contingencies depending on their nature.</p>	<p>The acquiree's contingent liabilities are recognized separately at the acquisition date, provided their fair values can be measured reliably. The contingent liability is measured subsequently at the higher of the amount initially recognized or the best estimate of the amount required to settle (under the provisions guidance).</p> <p>Contingent assets are not recognized.</p>

Impact	US GAAP	IFRS
<p>Assignment/allocation and impairment of goodwill</p> <p>The definition of the levels at which goodwill is assigned/allocated and tested for impairment varies between the two frameworks and may not be the same.</p> <p>Additional differences in the impairment testing methodologies could create further variability in the timing and extent of recognized impairment losses.</p>	<p>Goodwill is assigned to an entity's reporting units, as defined within the guidance.</p> <p>Goodwill impairment testing is performed under a two-step approach:</p> <ol style="list-style-type: none"> 1. The fair value and the carrying amount of the reporting unit, including goodwill, are compared. If the fair value of the reporting unit is less than the carrying amount, step 2 is completed to determine the amount of the goodwill impairment loss, if any. 2. Goodwill impairment is measured as the excess of the carrying amount of goodwill over its implied fair value. The implied fair value of goodwill—calculated in the same manner that goodwill is determined in a business combination—is the difference between the fair value of the reporting unit and the fair value of the various assets and liabilities included in the reporting unit. <p>Any loss recognized is not permitted to exceed the carrying amount of goodwill. The impairment charge is included in operating income.</p>	<p>Goodwill is allocated to a cash-generating unit (CGU) or group of CGUs, as defined within the guidance.</p> <p>Goodwill impairment testing is performed under a one-step approach:</p> <p>The recoverable amount of the CGU or group of CGUs (i.e., the higher of its fair value less costs to sell and its value in use) is compared with its carrying amount.</p> <p>Any impairment loss is recognized in operating results as the excess of the carrying amount over the recoverable amount.</p> <p>The impairment loss is allocated first to goodwill and then on a pro rata basis to the other assets of the CGU or group of CGUs to the extent that the impairment loss exceeds the book value of goodwill.</p>

Impact	US GAAP	IFRS
Other		
Noncontrolling interests Noncontrolling interests are measured at full fair value under US GAAP while IFRS provides two valuation options, which could result in differences in the carrying values of noncontrolling interests.	Noncontrolling interests are measured at fair value. In addition, no gains or losses are recognized in earnings for transactions between the parent company and the noncontrolling interests—unless control is lost.	Entities have an option, on a transaction-by-transaction basis, to measure noncontrolling interests at their proportion of the fair value of the identifiable net assets or at full fair value. The use of the full fair value option results in full goodwill being recorded on both the controlling and noncontrolling interest. In addition, no gains or losses will be recognized in earnings for transactions between the parent company and the noncontrolling interests—unless control is lost.
Combinations involving entities under common control Under US GAAP there are specific rules for common control transactions. IFRS provides more variability in the accounting treatment for such transactions.	Combinations of entities under common control are generally recorded at predecessor cost, reflecting the transferor's carrying amount of the assets and liabilities transferred.	IFRS does not specifically address such transactions. Entities develop and consistently apply an accounting policy; management can elect to apply purchase accounting or the predecessor value method to a business combination involving entities under common control. The accounting policy can be changed only when criteria for a change in an accounting policy are met in the applicable guidance (i.e., it provides more-reliable and more-relevant information). Related-party disclosures are used for explaining the impact of transactions with related parties.

Impact	US GAAP	IFRS
<p>Effective date and early application</p> <p>Significant GAAP differences may exist with respect to when the new guidance is adopted.</p>	<p>The new business combinations standard was effective for acquisitions that close in years beginning after December 15, 2008 (2009 for calendar year-end companies), and is to be applied prospectively.</p>	<p>IFRS 3 (Revised) is effective for acquisitions occurring in the first annual reporting period beginning on or after July 1, 2009, and is to be applied prospectively unless it is being applied in conjunction with a first-time adoption of IFRS.</p> <p>It can be applied early, but only to an annual period beginning on or after June 30, 2007, as long as IAS 27 (Revised) is also applied at the same time.</p>
<p>Identifying the acquirer</p> <p>Potentially different entities may be determined to be the acquirer when applying purchase accounting.</p> <p>Impacted entities should refer to the Consolidation section above for a more detailed discussion of differences related to the consolidation models between the frameworks that may create significant differences in this area.</p>	<p>The acquirer is determined by reference to ASC 810-10, under which the general guidance is that the party that holds directly or indirectly greater than 50 percent of the voting shares has control, unless the acquirer is the primary beneficiary of a VIE in accordance with ASC 810.</p>	<p>The acquirer is determined by reference to IAS 27 (Revised), under which the general guidance is the party that holds greater than 50 percent of the voting power has control. In addition, there are several instances where control may exist if less than 50 percent of the voting power is held by an entity. Neither IFRS 3 (Revised) nor IAS 27 (Revised) contains guidance related to primary beneficiaries.</p>

Impact	US GAAP	IFRS
Fair value When measuring the fair value of assets acquired and liabilities assumed, there are differences in the definitions of fair value between US GAAP and IFRS, which could result in different fair values of assets acquired and liabilities assumed including goodwill.	<p>Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The exchange price represents an exit price.</p> <p>A fair value measurement assumes that the transaction occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market.</p> <p>Fair value measurements include concept of “highest and best use,” which refers to how market participants would use an asset to maximize the value of the asset or group of assets. The highest and best use is determined based on the use of the asset by market participants, even if the intended use of the asset by the reporting entity is different.</p> <p>The fair value definition of a liability is based on a transfer concept and reflects nonperformance risk, which generally considers the entity’s own credit risk.</p>	<p>Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm’s-length transaction. IFRS does not specifically refer to either an entry or exit price</p> <p>IFRS does not contain guidance about which market should be used as a basis for measuring fair value when more than one market exists; however, under both IFRS and US GAAP, observable markets typically do not exist for many assets acquired in a business combination. As a result, for many nonfinancial assets, the principal or most advantageous market will be represented by a hypothetical market, which will likely be the same under both frameworks.</p> <p>IFRS does not include an equivalent valuation premise to “highest and best use” under US GAAP in measuring fair value.</p> <p>The fair value definition of a liability uses a settlement concept.</p> <p>The fair value of financial instruments should reflect the credit quality of the instrument, and generally the entity’s own credit risk. However, the fair value of nonfinancial liabilities may not necessarily consider the entity’s own credit risk.</p>
Employee benefit arrangements and income tax		
Accounting for share-based payments and income taxes in accordance with separate standards, not at fair value, may result in different results being recorded as part of purchase accounting.		

Impact	US GAAP	IFRS
Technical references		
IFRS	IAS 12, IAS 27 (Revised), IAS 38, IFRS 2, IFRS 3 (Revised)	
US GAAP	ASC 205-20, ASC 350-10, ASC 350-20, ASC 350-30, ASC 360-10, ASC 805, ASC 810, ASC 810-10	
PwC Guide <i>A Global Guide to Accounting for Business Combinations and Noncontrolling Interests</i>		

Note

The foregoing discussion captures a number of the more significant GAAP differences. It is important to note that the discussion is not inclusive of all GAAP differences in this area.

Recent/proposed guidance

IFRS

The IASB published an exposure draft on Fair Value Measurement for comment through September 2009. The exposure draft might affect the definition of fair value as currently contained in IFRS 3 (Revised). There are other ongoing projects on some standards that are linked to business combinations (notably, IAS 37 on provisions and IAS 12 on deferred tax) that may affect either the recognition or measurement at the acquisition date or the subsequent accounting.

Other accounting and reporting topics

Other accounting and reporting topics

In addition to areas previously discussed, differences exist in a multitude of other standards, including translation of foreign currency transactions, calculation of earnings per share, disclosures regarding operating segments and discontinued operations treatment. Differences also exist in the presentation and disclosure of annual and interim financial statements.

There are currently differences in the calculation of diluted earnings per share, which could result in differences in the amounts reported. Some of the differences (such as the inclusion of option grants, even in the instance where a company is prohibited from issuing new shares) would result in lower potential common shares under IFRS, while others (such as the presumption that contracts that can be settled in either cash or common shares will always settle in shares) would generally result in a higher number of potential common shares under IFRS.

IFRS contains a different definition of a discontinued operation than does US GAAP. The IFRS definition of a component—for purposes of determining whether a disposition would qualify for discontinued operations treatment—requires the unit to represent a separate major line of business or geographic area of operations or to be a subsidiary acquired exclusively with a view toward resale.

Differences in the guidance surrounding the offsetting of financial assets and liabilities under master netting arrangements, repurchase and reverse-repurchase arrangements and the number of parties involved in the offset arrangement could change the balance sheet presentation of items currently shown net (or gross) under US GAAP, which could impact an entity's key metrics or ratios.

Further details on the foregoing and other selected differences are described in the following table.

Impact	US GAAP	IFRS
Financial statements		
Balance sheet: offsetting assets and liabilities Differences in the guidance covering the offsetting of assets and liabilities under master netting arrangements, repurchase and reverse-repurchase arrangements and the number of parties involved in the offset arrangement could change the balance sheet presentation of items currently shown net (or gross) under US GAAP. Consequently, more items are likely to appear gross under IFRS.	The guidance states that "it is a general principle of accounting that the offsetting of assets and liabilities in the balance sheet is improper except where a right of setoff exists." A right of setoff is a debtor's legal right, by contract or otherwise, to discharge all or a portion of the debt owed to another party by applying against the debt an amount that the other party owes to the debtor. A debtor having a valid right of setoff may offset the related asset and liability and report the net amount. A right of setoff exists when all of the following conditions are met:	Under the guidance, a right of setoff is a debtor's legal right, by contract or otherwise, to settle or otherwise eliminate all or a portion of an amount due to a creditor by applying against that amount an amount due from the creditor. Two conditions must exist for an entity to offset a financial asset and a financial liability (and thus present the net amount on the balance sheet). The entity must:

Impact	US GAAP	IFRS
Balance sheet: offsetting assets and liabilities (continued)	<ul style="list-style-type: none"> Each of two parties owes the other determinable amounts. The reporting party has the right to set off the amount owed with the amount owed by the other party. The reporting party intends to set off. The right of setoff is enforceable by law. <p>Repurchase agreements and reverse-repurchase agreements that meet certain conditions are permitted, but not required, to be offset in the balance sheet.</p> <p>The guidance provides an exception to the previously described intent condition for derivative instruments executed with the same counterparty under a master netting arrangement. An entity may offset (1) fair value amounts recognized for derivative instruments and (2) fair value amounts (or amounts that approximate fair value) recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) arising from derivative instruments recognized at fair value. Entities must adopt an accounting policy to offset fair value amounts under this guidance and apply that policy consistently.</p>	<ul style="list-style-type: none"> Currently have a legally enforceable right to set off the recognized amounts; and Intend either to settle on a net basis or to realize the asset and settle the liability simultaneously. <p>In unusual circumstances, a debtor may have a legal right to apply an amount due from a third party against the amount due to a creditor, provided that there is an agreement among the three parties that clearly establishes the debtor's right of setoff.</p> <p>Master netting arrangements do not provide a basis for offsetting unless both of the criteria described earlier have been satisfied.</p>

Impact	US GAAP	IFRS
Balance sheet: classification Under IFRS, the classification of debt does not consider post-balance sheet refinancing agreements. As such, more debt is classified as current under IFRS.	<p>Entities may classify debt instruments due within the next 12 months as noncurrent at the balance sheet date, provided that agreements to refinance or to reschedule payments on a long-term basis (including waivers for certain debt covenants) get completed before the financial statements are issued.</p> <p>The presentation of a classified balance sheet is required, with the exception of certain industries.</p>	<p>If completed after the balance sheet date, neither an agreement to refinance or reschedule payments on a long-term basis nor the negotiation of a debt covenant waiver would result in noncurrent classification of debt, even if executed before the financial statements are issued.</p> <p>The presentation of a classified balance sheet is required, except when a liquidity presentation is more relevant.</p>
Income statement The most significant differences between the frameworks are, under IFRS, the ability to present expenses based on their nature, rather than their function, and the option of presenting all items of income and expense in either a single statement of comprehensive income or two statements (an income statement and a statement of comprehensive income). IFRS does not permit display of comprehensive income and its components in a statement of changes in equity, which is acceptable under US GAAP.	<p>The income statement can be presented in (1) either a single-step format, whereby all expenses are classified by function and then deducted from total income to arrive at income before tax or (2) a multiple-step format separating operating and nonoperating activities before presenting income before tax.</p> <p>SEC regulations require all registrants to categorize expenses in the income statement by their function. However, depreciation expense may be presented as a separate income statement line item. In such instances the caption cost of sales should be accompanied by the phrase <i>exclusive of depreciation</i> shown below and presentation of a gross margin subtotal is precluded.</p>	<p>Entities can present all items of income and expense in either a single statement of comprehensive income or two statements (an income statement and a statement of comprehensive income). Expenses can be presented either by function or by nature. Additional disclosure of expenses by nature is required if functional presentation is used.</p> <p>No prescribed statement of comprehensive income format exists. At least the following items have to be disclosed:</p> <ul style="list-style-type: none"> • Revenue • Finance costs • Share of post tax results of associates and joint ventures accounted for by the equity method • Tax expense • Post tax gain or loss attributable to the results and to remeasurement of discontinued operations

Impact	US GAAP	IFRS
Income statement (continued)	<p>Although US GAAP does not use the term <i>exceptional items</i>, significant unusual or infrequently occurring items are reported as components of income separate from continuing operations—either on the face of the statement of operations or in the notes to the financial statements.</p> <p>Extraordinary items are defined as being both infrequent and unusual and are rare in practice.</p>	<ul style="list-style-type: none"> • Profit or loss for the period • Each component of other comprehensive income classified by nature (except for share of other comprehensive income of associates and joint ventures accounted for using the equity method) • Share of other comprehensive income of associates and joint ventures accounted for using the equity method • Total comprehensive income <p>Entities that disclose an operating result should include all items of an operating nature, including those that occur irregularly or infrequently or are unusual in amount within that caption.</p> <p>Entities should not mix functional and nature classifications of expenses by excluding certain expenses from the functional classifications to which they relate.</p> <p>The term <i>exceptional items</i> is not used or defined. However, the separate disclosure is required (either on the face of the income statement or in the notes) of items of income and expense that are of such size, nature or incidence that their separate disclosure is necessary to explain the performance of the entity for the period.</p> <p>Extraordinary items are prohibited.</p>

Impact	US GAAP	IFRS
<p>Statements of equity and comprehensive earnings</p> <p>IFRS requires a statement of changes in equity to be presented as a primary statement for all entities.</p>	<p>Permits the statement of changes in shareholders' equity to be presented either as a primary statement or within the notes to the financial statements.</p> <p>Entities may utilize one of three formats in their presentation of comprehensive income:</p> <ul style="list-style-type: none"> • A single primary statement of income and comprehensive income • A two-statement approach (a statement of income and a statement of comprehensive income) • A separate category highlighted within the primary statement of changes in shareholders' equity 	<p>A statement of changes in equity is presented as a primary statement for all entities. At least the following items have to be presented:</p> <ul style="list-style-type: none"> • Total comprehensive income for the period, showing separately the total amounts attributable to owners of the parent and to minority interest • For each component of equity, the effects of retrospective application or retrospective restatement recognized in accordance with IAS 8 • The amounts of transactions with owners in their capacity as owners, showing separately contributions by and distributions to owners • For each component of equity, a reconciliation between the carrying amount at the beginning and the end of the period, separately disclosing each change

Impact	US GAAP	IFRS
<p>Statement of cash flows</p> <p>Differences exist between the two frameworks for the presentation of the statement of cash flows that could result in differences in the actual amount shown as cash and cash equivalents in the statement of cash flows as well as changes to each of the operating, investing and financing sections of the statement of cash flows.</p>	<p>Bank overdrafts are not included in cash and cash equivalents; changes in the balances of overdrafts are classified as financing cash flows, rather than being included within cash and cash equivalents.</p> <p>The guidance is specific on the cash flow classification of certain items, requiring dividends paid to be classified in the financing section of the cash flow statement and requiring interest paid, interest received and dividends received to be classified as cash flows from operations. Taxes paid are generally classified as operating cash flows; specific rules exist regarding the classification of the tax benefit associated with share-based compensation arrangements.</p> <p>Additional disclosure rules exist regarding the supplemental disclosure of interest and taxes paid during the period at the foot of the cash flow statement.</p>	<p>Cash may also include bank overdrafts repayable on demand. Short-term bank borrowings are not included in cash or cash equivalents and are considered to be financing cash flows.</p> <p>Interest and dividends paid should be classified in either operating or financing cash flows; receipts of interest or dividends should be classified in either operating or investing activities. Taxes paid should be classified within operating cash flows unless specific identification with a financing or investing activity exists. Once an accounting policy election is made, it should be followed consistently.</p>

Impact	US GAAP	IFRS
<p>Disclosure of critical accounting policies and significant estimates</p> <p>An increased prominence exists in the disclosure of an entity's critical accounting policies and disclosures of significant accounting estimates under IFRS in relation to the requirements of US GAAP.</p>	<p>For SEC registrants, disclosure of the application of critical accounting policies and significant estimates is normally made in the Management's Discussion and Analysis section of Form 10-K.</p> <p>Financial statements prepared under US GAAP include a summary of significant accounting policies used within the notes to the financial statements.</p>	<p>Within the notes to the financial statements, entities are required to disclose:</p> <ul style="list-style-type: none"> • The judgments that management has made in the process of applying its accounting policies that have the most significant effect on the amounts recognized in those financial statements; and • Information about the key assumptions concerning the future—and other key sources of estimation uncertainty at the balance sheet date—that have significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.
<p>Comparative financial information</p> <p>IFRS specifies the periods for which comparative financial information is required, which differs from both US GAAP and SEC requirements.</p>	<p>Comparative financial statements are not required; however, SEC requirements specify that most registrants provide two years of comparatives for all statements except for the balance sheet, which requires only one comparative year.</p>	<p>One year of comparatives is required for all numerical information in the financial statements, with limited exceptions in disclosures. In limited note disclosures, more than one year of comparative information is required.</p> <p>A third balance sheet is also required for first-time adopters of IFRS and in situations where a restatement or reclassification has occurred. Reclassifications in this context are in relation to a change in accounting policies or accounting estimates, errors or changes in presentation of previously issued financial statements.</p>

Impact	US GAAP	IFRS
Earnings per share		
<p>Diluted earnings-per-share calculation</p> <p>Several specific differences currently exist that could result in a different denominator being utilized in the diluted earnings-per-share (EPS) calculation under the two frameworks.</p>	<p>In computing diluted EPS, the treasury stock method is applied to instruments such as options and warrants. This requires that the number of incremental shares applicable to the contract be included in the EPS denominator by computing a year-to-date weighted-average number of incremental shares by using the incremental shares from each quarterly diluted EPS computation. The if-converted method applies to most convertible securities, which requires the denominator to be adjusted under the assumption that all potential common shares under the contract are issued at the beginning of the period.</p> <p>Certain convertible debt securities give the issuer a choice of either cash or share settlement. These contracts would typically follow the if-converted method, as US GAAP contains the presumption that contracts that may be settled in common shares or in cash at the election of the entity will be settled in common shares. However, that presumption may be overcome if past experience or a stated policy provides a reasonable basis to believe it is probable that the contract will be paid in cash, in which case the treasury stock method is applied.</p>	<p>The guidance states that dilutive potential common shares shall be determined independently for each period presented, not a weighted average of the dilutive potential common shares included in each interim computation.</p> <p>The contracts that can be settled in either common shares or cash at the election of the entity or the holder are always presumed to be settled in common shares and included in diluted EPS; that presumption may not be rebutted.</p> <p>The potential common shares arising from contingently convertible debt securities would be included in the dilutive EPS computation only if the contingency price was met as of the reporting date.</p>

Impact	US GAAP	IFRS
Diluted earnings-per-share calculation (continued)	<p>Contingently convertible debt securities with a market price trigger (e.g., debt instruments that contain a conversion feature that is triggered upon an entity's stock price reaching a predetermined price) should always be included in diluted EPS computations if dilutive—regardless of whether the market price trigger has been met. That is, the contingency feature should be ignored.</p>	
Foreign currency translation		
Trigger to release amounts recorded in a currency translation account	<p>Different recognition triggers for amounts captured in a currency translation account (CTA) could result in more instances where amounts included in a CTA are recycled through the income statement under IFRS compared to US GAAP.</p> <p>Some or all of the CTA balance is released into the income statement in the following situations where a parent sells its interest or its interest is diluted via the foreign operation's share issuance:</p> <ul style="list-style-type: none"> • When control of a foreign subsidiary is lost, the entire CTA balance is released. • Complete liquidation of a foreign operation triggers full release of CTA. • When an interest is sold but significant influence is retained, a proportion of CTA is released. • When significant influence is lost, a proportion of CTA is released into the income statement and the remaining CTA balance affects the cost basis of the investment retained. <p>Amounts in the CTA should generally not be released into earnings when a first-tier foreign subsidiary sells or liquidates a second-tier subsidiary because the first-tier subsidiary still contains investments in foreign assets. This principle may be overcome in certain cases.</p>	<p>The triggers for sale and dilution noted in the US GAAP column apply for IFRS, except when significant influence is lost, the entire CTA balance is released into the income statement.</p> <p>Also, the sale of a second-tier subsidiary will trigger the release of CTA associated with that second-tier subsidiary even though ownership in the first-tier subsidiary has not been affected.</p>

Impact	US GAAP	IFRS
Translation in consolidated financial statements IFRS does not require equity accounts to be translated at historical rates.	Equity is required to be translated at historical rates.	Management has a policy choice to use either the historical rate or the closing rate. The chosen policy should be applied consistently. If the closing rate is used, the resulting exchange differences are recognized in equity and thus the policy choice has no impact on the amount of total equity.
Determination of functional currency Under US GAAP there is no hierarchy of indicators to determine the functional currency of an entity, whereas a hierarchy exists under IFRS.	There is no hierarchy of indicators to determine the functional currency of an entity. In those instances in which the indicators are mixed and the functional currency is not obvious, management's judgment is required so as to determine the currency that most faithfully portrays the primary economic environment of the entity's operations.	Primary and secondary indicators should be considered in the determination of the functional currency of an entity. If indicators are mixed and the functional currency is not obvious, management should use its judgment to determine the functional currency that most faithfully represents the economic results of the entity's operations by focusing on the currency of the economy that determines the pricing of transactions (not the currency in which transactions are denominated). Additional evidence (secondary in priority) may be provided from the currency in which funds from financing activities are generated or receipts from operating activities are usually retained, as well as from the nature of the activities and the extent of transactions between the foreign operation and the reporting entity.

Impact	US GAAP	IFRS
<p>Other</p> <p>Interim financial reporting—allocation of costs in interim periods</p> <p>IFRS requires entities to account for interim financial statements via the discrete-period method. The spreading of costs that affect the full year is not appropriate. This could result in increased volatility in interim financial statements.</p> <p>The tax charge in both frameworks is based on an estimate of the annual effective tax rate applied to the interim results plus the inclusion of discrete income tax-related events during the quarter in which they occur.</p>	<p>US GAAP views interim periods primarily as integral parts of an annual cycle. As such, it allows entities to allocate among the interim periods certain costs that benefit more than one of those periods.</p>	<p>Interim financial statements are prepared via the discrete-period approach, wherein the interim period is viewed as a separate and distinct accounting period, rather than as part of an annual cycle.</p>

Impact	US GAAP	IFRS
<p>Definition of discontinued operations</p> <p>The definitions of discontinued operations are different under IFRS compared to US GAAP. Therefore disposal transactions may be accounted for differently.</p>	<p>The results of operations of a component of an entity that either has been disposed of or is classified as held for sale are reported as discontinued operations if:</p> <ul style="list-style-type: none"> • The operations and cash flows have been or will be eliminated from the ongoing operations of the entity; and • There will be no significant continuing involvement in the operations of the component after the disposal transaction. <p>A component presented as a discontinued operation under US GAAP may be a reportable segment, operating segment, reporting unit, subsidiary or asset group.</p> <p>Generally, partial disposals characterized by movement from a controlling to a noncontrolling interest would not qualify as discontinued operations due to continuing involvement.</p>	<p>A discontinued operation is a component of an entity (operations and cash flows that can be clearly distinguished, operationally and for financial reporting, from the rest of the entity) that either has been disposed of or is classified as held for sale and represents a separate major line of business or geographic area of operations, or is a subsidiary acquired exclusively with a view to resale.</p> <p>Partial disposals characterized by movement from a controlling to a noncontrolling interest could qualify as discontinued operations.</p>

Impact	US GAAP	IFRS
Related parties—disclosure of management compensation Under IFRS, a financial statement requirement exists to disclose the compensation of key management personnel.	Disclosure of the compensation of key management personnel is not required within the financial statements. SEC regulations require key management compensation to be disclosed outside the primary financial statements.	The compensation of key management personnel is disclosed within the financial statements in total and by category of compensation.
Operating segments—segment reporting A principles-based approach to the determination of operating segments in a matrix-style organizational structure could result in entities disclosing different operating segments.	Entities that utilize a matrix form of organizational structure are required to determine their operating segments on the basis of products or services offered, rather than geography or other metrics.	Entities that utilize a matrix form of organizational structure are required to determine their operating segments by reference to the core principle (i.e., an entity shall disclose information to enable users of its financial statements to evaluate the nature and financial effects of the business activities in which it engages and the economic environments in which it operates).
Technical references		
IFRS	IAS 1, IAS 14, IAS 21, IAS 24, IAS 33, IFRS 5, IFRS 8	
US GAAP	ASC 205, ASC 205-20, ASC 230, ASC 260, ASC 280, ASC 360-10, ASC 830, ASC 830-30-40-2 to 40-4, ASC 850	

Note

The foregoing discussion captures a number of the more significant GAAP differences. It is important to note that the discussion is not inclusive of all GAAP differences in this area.

Recent/proposed guidance

Joint FASB/IASB Exposure Draft: *Simplifying Earnings Per Share*

In August 2008, a joint exposure draft was issued to reduce differences between IFRSs and US GAAP that can be resolved in a relatively short time and can be addressed outside major projects. The objective of the Earnings per Share project is to simplify and converge the calculation of EPS according to IAS 33, *Earnings per Share* and ASC 260, *Earnings per Share*. The project would help to eliminate differences in the denominator of the earnings per share calculation. As such, many of the existing differences will be eliminated if adopted as currently drafted. In April 2009, the IASB considered comments received in relation to the exposure draft. In light of other priorities, the IASB does not expect to discuss this project further until 2010.

Joint FASB/IASB Discussion Paper: *Preliminary Views on Financial Statement Presentation*

In October 2008, a joint discussion paper was issued with a goal of converging financial statement presentation. The purpose of this joint project is to establish a standard that will guide the organization and presentation of information in the financial statements. The result of this project will directly affect how the management of an entity communicates financial statement information to users of financial statements, such as present and potential equity investors, lenders, and other creditors. The proposal seeks to improve the usefulness of the information provided in an entity's financial statements to help users make decisions in their capacity as capital providers. The proposed model will require management judgment, will have a significant impact on financial statement presentation, and will eliminate existing financial statement presentation differences between US GAAP and IFRS. The discussion paper puts forth a model wherein companies would be required to:

- Classify assets, liabilities, income, expenses and cash flows as business or financing activities. Business activities would be further separated between operating and investing activities.
- Display income taxes, discontinued operations, and other comprehensive income separately from the business and financing categories.
- Prepare a line-by-line reconciliation between the cash flow statement and the statement of comprehensive income that separates fair value changes and other accruals from cash movements.
- Use the “direct method” for preparing the cash flow statement.

The Boards are currently reviewing responses to the discussion paper, with a goal of issuing an exposure draft in 2010.

Joint FASB/IASB Exposure Draft: *Discontinued Operations*

In September 2008, the Boards issued a joint exposure draft to develop a converged definition of a discontinued operation along with converged disclosure requirements for all components of an entity that have been (or will be) disposed of. As currently proposed, this will eliminate many of the differences that currently exist between US GAAP and IFRS in this area. The Boards are in the process of reviewing comments received in January 2009 and expect to issue a final standard in late 2009.

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IFRS for small and medium-sized entities

IFRS for small and medium-sized entities

In July 2009, the IASB released IFRS for Small and Medium-sized Entities (SMEs), which provides an alternative accounting framework for entities meeting certain eligibility criteria. IFRS for SMEs is a self-contained, comprehensive set of standards specifically designed for entities that do not have public accountability.

This section is intended to provide an overview of IFRS for SMEs, its eligibility criteria, and some examples of the differences between IFRS for SMEs, full IFRS, and US GAAP. For an in-depth comparison of IFRS for SMEs and full IFRS, please refer to the PwC publication *Similarities and differences—a comparison of ‘full IFRS’ and IFRS for SMEs*. In addition, a forthcoming PwC publication will explore the differences between IFRS for SMEs and US GAAP.

What companies can use IFRS for SMEs?

The IASB has determined that any entity that does not have public accountability can use IFRS for SMEs. An entity has public accountability if its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market, or if it holds assets in a fiduciary capacity for a broad group of outsiders—for example, a bank, insurance entity, pension fund, securities broker/dealer. The definition of a SME is therefore based on the nature of the entity rather than on its size.

To clarify, a subsidiary of a listed company that uses full IFRS would be eligible to use IFRS for SMEs provided that the subsidiary itself was not publicly accountable. However, for consolidation purposes, a subsidiary using IFRS for SMEs would then need to convert their financial statements to full IFRS, as the two accounting frameworks are not completely compatible for consolidation.

Beyond the scope of eligibility determined by the IASB, companies are also subject to the laws of their local jurisdiction. Many countries require statutory reporting, and each country will individually decide whether IFRS for SMEs is an acceptable basis for such reporting. Some countries that use full IFRS for public company reporting are considering proposals to replace their local GAAP with IFRS for SMEs (e.g., the UK), while others currently have no plans to allow use of IFRS for SMEs for statutory purposes (e.g., France). Companies will need to understand on a country-by-country basis where IFRS for SMEs will be allowed or required for statutory reporting.

What are some of the differences between full IFRS and IFRS for SMEs?

IFRS for SMEs retains many of the principles of full IFRS, but simplifies a number of areas that are generally less complicated or not relevant for small and medium-sized entities. In addition, IFRS for SMEs significantly streamlines the volume and depth of disclosures required by full IFRS, yielding a complement of disclosures that are more user-friendly for private entity stakeholders.

Certain areas deemed less relevant to SMEs, including earnings per share, segment reporting, insurance, and interim financial reporting, are completely omitted from the IFRS for SMEs guidance. In other instances, certain full IFRS principles were simplified to be more relevant and less cumbersome for private entities to apply. Some examples of the differences between full IFRS and IFRS for SMEs include:

Business combinations—Under full IFRS, transaction costs are excluded from the purchase price allocation (i.e., expensed as incurred), and contingent consideration is recognized regardless of the probability of payment. Under IFRS for SMEs, transaction costs are included in the purchase price allocation (i.e., cost of acquisition), and contingent consideration is recognized only if it is probable the amount will be paid and its fair value can be reliably measured.

Investments in associates—Under full IFRS, investments in associates are accounted for using the equity method. Under IFRS for SMEs, investments in associates can be accounted for under the cost method, equity method, or at fair value through profit and loss.

Goodwill and indefinite-lived intangibles—Under full IFRS, goodwill and indefinite-lived intangible assets must be tested at least annually for impairment, or when an indicator of impairment exists. Under IFRS for SMEs, there is no concept of indefinite-lived intangible assets. Therefore, goodwill and intangible assets are amortized over the useful life of the asset or 10 years (if the useful life cannot be determined). Goodwill and intangible assets are also tested for impairment only when an indicator of impairment exists.

Uncertain tax positions (UTPs)—There is no specific guidance on UTPs within the full IFRS income tax standard. However, under the general principles the UTP liability is recorded if the likelihood of payment is greater than 50 percent and is measured as either the single best estimate, or a weighted average probability of the possible outcomes. Under IFRS for SMEs, the liability is measured using the probability weighted average amount of all possible outcomes. There is no probable recognition threshold.

Research & development costs—Under full IFRS, research costs are expensed while development costs meeting certain criteria are capitalized. Under IFRS for SMEs, all research and development costs are expensed.

What are some of the differences between US GAAP and IFRS for SMEs?

In areas where US GAAP and IFRS are mostly converged (e.g., business combinations), the differences between US GAAP and IFRS for SMEs will likely seem very similar to the differences noted above between full IFRS and IFRS for SMEs. However, there are other examples of differences between US GAAP and IFRS for SMEs:

Inventory—Under US GAAP, LIFO is an acceptable method of valuing inventory. In addition, impairments to inventory value are permanent. Under IFRS for SMEs, use of LIFO is not allowed, and impairments of inventory can be reversed under certain circumstances.

Provisions—Under US GAAP, a provision is recorded if it is probable (generally regarded as 75 percent or greater) that an outflow will occur. If no best estimate of the outflow is determinable, but a range of possibilities exist, the lowest point on the

range is the value that should be recorded. Under IFRS for SMEs, a provision is recorded if it is more likely than not (generally considered to be greater than 50 percent) that an outflow will occur. If no best estimate of the outflow is determinable, but a range of possibilities exist, the midpoint should be recorded.

Borrowing costs—US GAAP requires capitalization of borrowing costs directly attributable to the acquisition, construction or production of qualifying assets. Under IFRS for SMEs, all borrowing costs must be expensed.

Equity instruments—Under US GAAP, complex equity instruments such as puttable stock and mandatorily redeemable preferred shares can qualify as equity (or mezzanine equity), particularly for private companies. Under IFRS for SMEs, these types of instruments are more likely to be classified as a liability, depending on the specifics of the individual instrument.

Revenue on construction-type contracts—Under US GAAP, the percentage of completion method is preferable though the completed contract method is required in certain situations. Under IFRS for SMEs, the completed contract method is prohibited.

How can I learn more?

For an in-depth comparison of IFRS for SMEs and full IFRS, please refer to the PwC publication *Similarities and differences—a comparison of ‘full IFRS’ and IFRS for SMEs*. In addition, a forthcoming PwC publication will explore the differences between IFRS for SMEs and US GAAP.

FASB Codification

FASB Codification

On July 1, 2009, the Financial Accounting Standards Board Codification of US GAAP was launched as the sole source of authoritative non-governmental US GAAP. *The FASB Accounting Standards Codification™* (the “Codification”) is effective for financial statements that cover interim and annual periods ending after September 15, 2009. Other than resolving certain minor inconsistencies in current US GAAP, the Codification is not supposed to change US GAAP. The Codification is a new structure that takes accounting pronouncements and organizes them by accounting topic. Users can select a topic and gain access to all the guidance that should be applicable to that topic.

All guidance in the Codification is considered authoritative on July 1, 2009. There will then be two levels of US GAAP, authoritative and nonauthoritative. The FASB will no longer issue FASB Statements, FASB Staff Positions (FSPs), FASB Interpretations (FINs), or Emerging Issues Task Force (EITF) Abstracts. As updates are made, they will be numbered so constituents can track the updates. For example, for 2009, the updates will be numbered 2009-01, 2009-02, 2009-03, etc.

Given the changes described above, the Codification will affect the way companies reference US GAAP in financial statements and in their accounting policies.

Codification content

The Codification includes all standards issued by a standard setter within levels A through D of the current GAAP hierarchy, as defined by Statement on Auditing Standards No. 69, *The Meaning of “Present Fairly in Conformity with Generally Accepted Accounting Principles.”* This includes standards such as:

- FASB Statements (including Basis for Conclusion), Interpretations, and Technical Bulletins
- EITF Abstracts
- Derivative Implementation Group (DIG) Issues
- Accounting Principles Board (APB) Opinions
- American Institute of Certified Public Accountants (AICPA) Statements of Position (SOP)

To increase the usefulness of the Codification for public companies, relevant authoritative guidance issued by the SEC, and selected SEC staff interpretations and administrative guidance is also included in the Codification, such as:

- Regulation S-X
- Financial Reporting Releases/Accounting Series Releases
- Interpretive Releases
- SEC Staff guidance in Staff Accounting Bulletins, EITF Topic D, and SEC Staff Observer comments made at meetings of the EITF

Items excluded from Codification

The Codification does not contain all SEC guidance. For example, it does not include content related to matters outside of the basic financial statements, such as Management's Discussion and Analysis (MD&A), auditing, or independence matters.

The following has also been excluded from the Codification:

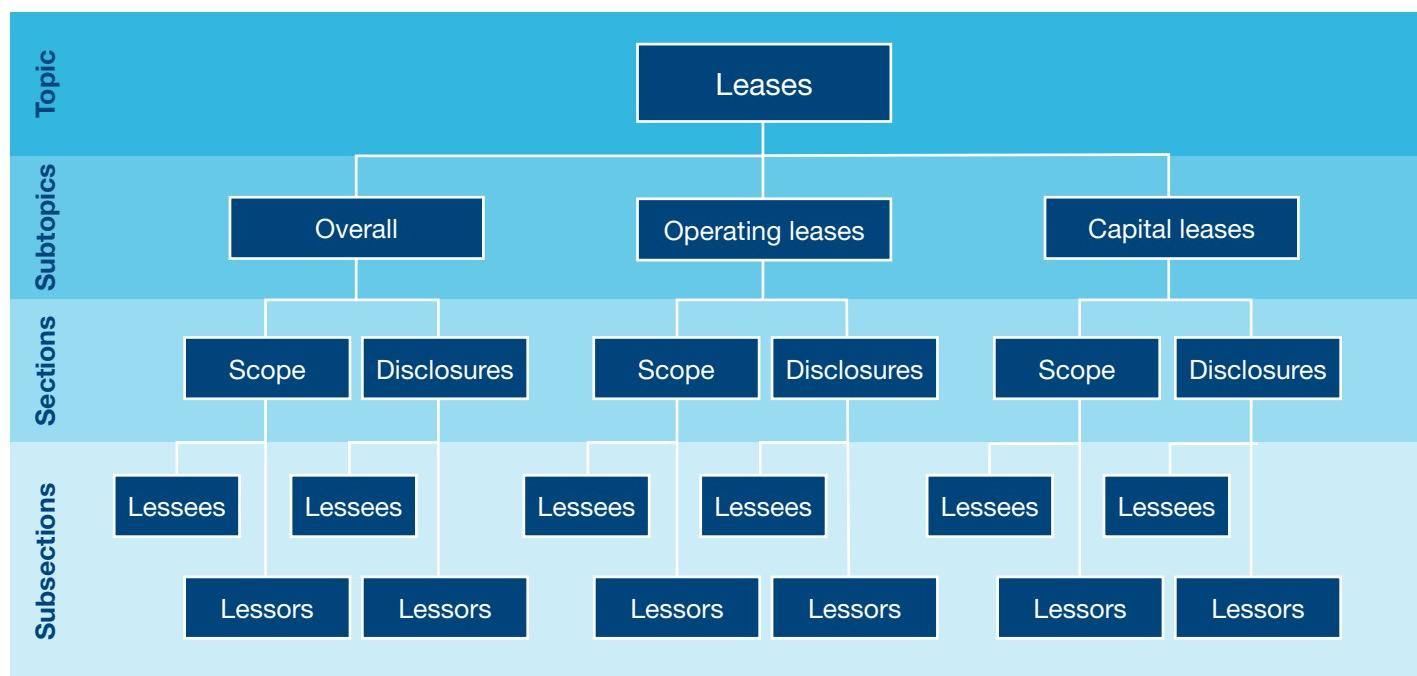
- Standards that are outdated or superseded by December 31, 2008
- All governmental accounting standards
- Grandfathered materials (Grandfathered materials will only be accessible in original standards. Some examples of grandfathered materials not included in the Codification are: pooling of interests in a business combination, qualifying special-purpose entities, and pension transition assets or obligations.)

Codification format

The Codification is presented in a hierarchy with four basic levels: Topics, Subtopics, Sections, and Subsections. Topics are aggregated into the following common areas:

- Presentation (e.g., balance sheet, income statement, statement of cash flows, and notes to financial statements)
- Financial statement accounts (e.g., assets, liabilities, equity, revenue, and expense), which include topics such as cash, receivables, debt, revenue recognition and income taxes
- Broad transactions, which include topics such as business combinations, derivatives and hedging, and leases, and
- Industry-specific guidance, which provides additional guidance specific to particular industries, such as airlines, entertainment and real estate

The following figure provides the terminology and a visual representation using a partial hierarchy of the Leases Topic:



Note: This is for illustrative purposes only and does not include all Topics, Subtopics, Sections and Subsections.

The following is a summary table of contents for the FASB Codification.

FASB Accounting Standards Codification™— Table of Contents (Topic Level)

Notice to Constituents

General Principles

105 *Generally Accepted Accounting Principles*

Presentation

205 *Presentation of Financial Statements*

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215 *Statement of Shareholder Equity*

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32X *Investments*

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340 *Deferred Costs and Other Assets*

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360 *Property, Plant, and Equipment*

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405 *Liabilities*

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420 *Exit or Disposal Cost Obligations*

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Exposure Drafts

Codification Updates

FASB/IASB project summary exhibit

FASB/IASB project summary exhibit

The following table presents the status of all joint projects on the agenda of the IASB and FASB. In addition, each board separately has a number of research and standards projects in various stages of completion. Although preliminary in some cases, the topics under consideration provide an overview of and insight into how each set of standards may further evolve. More information on the status of these projects can be found on each Board's web site. For the IASB, visit www.iasb.org. For the FASB, visit www.fasb.org.

	Responsible Board	2009	2010	Years thereafter
		Issuance anticipated	Issuance anticipated	Timing to be determined

Joint projects

Standards and amendment to standards

Consolidation (portion relating to IASB active agenda)	Joint	F		
Earnings per share	FASB IASB			TBD TBD
Emissions trading schemes	Joint		ED	F 2011
Financial statement presentation	Joint		ED	F 2011
Phase B				TBD
Phase C				
Derecognition	FASB IASB		F	TBD
Fair value measurement guidance	Joint	ED	F	
Income tax	FASB IASB	ED	F	TBD
Leases	Joint		ED	F 2011
Revenue recognition	Joint		ED	F 2011
Amendments to IFRS 5: Noncurrent assets held for sale and discontinued operations/FAS 144: Reporting discontinued operations	Joint	F		
Financial instruments with characteristics of equity	Joint		ED	F 2011
Hedging	FASB IASB	ED	F	TBD

	Responsible Board	2009 Issuance anticipated	2010 Issuance anticipated	Years thereafter Timing to be determined
Financial instruments—improvements to recognition and measurement	FASB IASB		ED/F ED	
Classification and measurement Impairment		ED/F ED	F	
Insurance contracts	Joint	ED		F 2011
Conceptual framework				
Phase A: Objectives and qualitative characteristics	Joint	F		
Phase B: Elements and recognition	Joint		DP	TBD
Phase C: Measurement	FASB IASB	DP DP	ED	TBD F 2011
Phase D: Reporting entity	Joint	ED	F	
Phase E: Presentation and disclosure	Joint			TBD
Phase F: Framework purpose and status in GAAP hierarchy	Joint			TBD
Phase G: Application to not-for-profit entities	Joint			TBD
Phase H: Remaining issues/entire framework	Joint			TBD
Other IASB projects				
Annual improvements—2010 cycle	IASB	ED	F	
First-time adoption of IFRSs (IFRS 1): Additional exemptions	IASB	F		
Joint ventures (IAS 37 amendments)	IASB	F		
Liabilities	IASB	ED or F		
Management commentary	IASB	ED	F	
Post employment benefits, including pensions	IASB			
Discount rate		ED/F		
Recognition and measurement		ED		F 2011
Related party disclosures	IASB	F		
Credit risk in liability measurement	IASB	DP		
Rate-regulated activities	IASB	ED	F	

	Responsible Board	2009	2010	Years thereafter
		Issuance anticipated	Issuance anticipated	Timing to be determined
Amendment to IFRIC 14—The limit on a defined benefit asset minimum funding requirements and their interaction	IASB	ED/F		
Classification of rights issues	IASB	ED/F		

IASB research agenda

Extractive activities	IASB	DP		TBD
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FASB research and other FASB projects**FASB research projects**

Financial instruments—derecognition	Joint			TBD
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Other FASB projects

Consolidations: policy and procedure	Joint	ED	F	
Oil and gas disclosures	FASB	ED/F		
Disclosure of certain loss contingencies	FASB	F		
Disclosure framework	FASB		DP	TBD
Deferred tax assets and liabilities on available-for-sale debt securities that are expected to be held to recovery	FASB			TBD
Loan loss disclosures	FASB	F		
Technical corrections to FASB statements and other US GAAP literature	FASB	F		
Going concern	FASB	ED/F		
Postretirement benefit obligations including pensions (Phase 2)	FASB			TBD
Treatment of base jackpot liabilities of casinos	FASB	ED	F	

	Responsible Board	2009 Issuance anticipated	2010 Issuance anticipated	Years thereafter Timing to be determined
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FASB staff positions and other activities

Embedded credit derivatives scope exception (DIG Issue C-22)	FASB	ED/F		
Recoveries of other-than-temporary impairments (reversals)	FASB			TBD
FAS 157—Measuring liabilities under FASB Statement no. 157 (proposed FSP FAS 157-c)	FASB	F		
FAS 157—Applying fair value to interest in alternative investments (proposed FSP FAS 157-g)	FASB	F		
FAS 157—Improving disclosures about fair value measurements	FASB	ED/F		
FIN 48—Applicability for private entities: Pass-through entities and amendments to existing disclosure requirements (Phase 2)	FASB	F		
Reconsideration of the scope of FAS 160	FASB	ED/F		

Explanation of symbols:

D = Draft

DP = Discussion Paper

ED = Exposure Draft

F= Final

TBD = To be determined

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Our US IFRS site contains a wealth of information and tools on where we currently stand and what companies should be doing in the US. Resources include our “IFRS First” newsletter, extensive publications, in-depth webcast series, Video Learning Center, and other interactive tools. Designed primarily with first-time adopters of IFRS in mind.

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